IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

SPECIAL CIVIL APPLICATION NO. 17040 of 2012

With

WRIT PETITION (PIL) NO. 211 of 2012

FOR APPROVAL AND SIGNATURE:

HONOURABLE THE CHIEF JUSTICE MR. BHASKAR BHATTACHARYA
and

HONOURABLE MR.JUSTICE J.B.PARDIWALA

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1 Whether Reporters of Local Papers may be allowed to see the judgment ?

2 To be referred to the Reporter or not ?

3 Whether their Lordships wish to see the fair copy of the judgment ?

4 Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 or any order made thereunder ?

5 Whether it is to be circulated to the civil judge ?

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NIKHIL T PARIKH - SOLE PROPREITOR OF PARIKH & PARIKH & 55....Petitioner(s)

Versus

UNION OF INDIA THRO SECRETARY & 14....Respondent(s)

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Appearance:
MR MIHIR THAKORE, SR.ADVOCATE with MS AMRITA M THAKORE, ADVOCATE for the Petitioner(s) No. 1 - 56
MR ANSHIN H DESAI, ADVOCATE for the Respondent(s) No. 1

MR SN SHELAT, SR.ADVOCATE with MS DHARMISHTA RAVAL, ADVOCATE for the Respondent(s) No. 2
MS. SHAILI A KAPADIA, ADVOCATE for the Respondent(s) No. 3
NOTICE SERVED for the Respondent(s) No. 5 - 12 , 15
NOTICE UNSERVED for the Respondent(s) No. 4 , 13 - 14
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CORAM: **HONOURABLE THE CHIEF JUSTICE MR. BHASKAR BHATTACHARYA**
and
HONOURABLE MR.JUSTICE J.B.PARDIWALA

Date : 07/05/2014

CAV JUDGEMENT
(PER : HONOURABLE MR.JUSTICE J.B.PARDIWALA)

As the issues raised in both the above captioned petitions are the same, those were heard analogously and are being disposed of by this common judgment and order. However, we have considered the Special Civil Application No.17040 of 2012 filed by the Trading Members and shareholders of the Vadodara Stock Exchange Limited as the lead matter.

By this writ application under Article 226 of the Constitution of India, the petitioners herein claiming to be the Trading Members and shareholders of the Vadodara Stock Exchange Limited (for short, 'VSEL') seeks to challenge the legality and validity of the circulars dated 30th May 2012 and 13th December 2012 and the Securities Contracts (Regulation)

(Stock Exchange and Clearing Corporations) Regulations, 2012, issued by the Securities Exchange Board of India (for short, 'SEBI') including the notice dated 28th November 2012 issued by the VSEL on the grounds, *inter alia,* that the impugned circulars, regulations and notice are *ultra vires* the Constitution of India and are contrary to the provisions of the Securities Contracts (Regulation) Act, 1956 and the Companies Act, 1956.

According to the petitioners, they are Trading Members and shareholders of the VSEL and have preferred the petition in their personal capacity as the Trading Members and also as a representative petition on behalf of the other Trading Members of the VSEL.

The respondent no.1 is the Union of India. The respondent no.2 is the Securities and Exchange Board of India established under the Securities and Exchange Board of India Act, 1992 (for short, 'SEBI Act') for the purpose of carrying out the functions assigned to it under the Securities Contracts (Regulation) Act, 1956 (for short, 'SCRA') and the SEBI Act. The respondent no.3 is the Vadodara Stock Exchange Limited of which the petitioners are Trading Members and shareholders.

The case made out by the petitioner in this petition may be summarised as under :

The VSEL, an RSE (Regional Stock Exchange) was established in the year 1990 as a company limited by guarantee. Initially, in Stock Exchanges all over the world including India, ownership and trading rights were vested upon the Trading Members of the Stock Exchanges. The VSEL was also established in the same manner and got recognition from the Government of India in the year 1990. Today, the VSEL has 289 Trading Members and 456 listed companies, out of which, 59 are exclusively listed on it. Until the expansion of the terminals of the BSE and NSE all over India, the VSEL was one of the most successful RSEs in India. In or around the year 1996-97, the turnover of the VSEL was in the range of approximately Rs.10 to 15 crore per day. Considering the share prices in those times (which would have been only 10 to 20% of today’s prices) and considering the fact that, this was prior to dematerialisation of securities in the year 2000 which led to enormous increase in trading of securities, the said per day turnover figures can be said to be enormous for those times.

Since its inception, the VSEL has initiated several steps to establish and upgrade its systems and infrastructure keeping the interest of investors in mind and in order to expand its activities. The VSEL introduced computerised system for settlement of transactions and installed systems to disseminate vital and timely information of price movement of various scrips to the investors and also set up the Investor Protection Fund to ensure increased protection of customers. Pursuant to reforms introduced whereby corporate membership in Stock Exchanges was introduced, the VSEL admitted corporate members. Recognising and appreciating the necessity of introducing Screen Based Trading at Vadodara which required a large premises, the VSEL acquired and owns a nine-storey-building having an aggregate area of 156238 sq.ft. in Vadodara and another premises *admeasuring* 4183 sq.ft. also at Vadodara. In 1996, the VSEL went live for electronic trading. Thereafter, the VSEL signed an agreement with one CMC Limited for implementing fully automated stock trading, settlement and clearing system. The VSEL has actively focused on empowerment of investors by establishing Investor Services Centres, Investor Education/Training Centre, Investor Information Centre, well-equipped library, etc. It has also developed advanced technological systems for its operations.

In or around the period between 1996 and 1998, due to the expansion of terminals of the NSE and BSE all over the country, the trading volume at all the RSEs, including the VSEL, started dwindling. In order to revive the fortunes of the RSEs, the SEBI issued a circular dated 26th November 1999 (subsequently modified by circular dated 16th December 1999) permitting the RSEs to acquire the membership of the NSE and BSE by floating a subsidiary company which would be permitted to acquire membership rights in the BSE and NSE. According to the provisions of the said circular, members of the Stock Exchange were required to register themselves as sub-brokers of the subsidiary to enable them trade through the subsidiary.

Pursuant to this, in the year 2000, the VSEL established and promoted a subsidiary company called ‘VSE Stock Services Limited’ ('VSSL') for acquiring membership of the BSE and NSE. The VSSL is a professionally managed trading and clearing member in cash segment of the BSE and NSE. The VSSL has had an annual turnover of Rs.22,317 crore in FY 2009-2010, Rs.17,639 crore in FY 2010-2011 and Rs.11,932 crore in FY 2011-2012. In fact, since its incorporation in the year 2000, the

VSSL has consistently had a very large turnover every year.

Many RSEs, including the VSEL, had their own trading platforms which were operational prior to the onslaught of nationwide terminals of the BSE and NSE after which they became non-operational on account of their not being able to sustain themselves in competition with national level players like the BSE and NSE. Due to the dwindling fortunes of the RSEs pursuant to the expansion of the BSE and NSE terminals, in 2004, an amendment was made to Section 13 of the SCRA on account of which the RSEs could enter into a Memorandum of Understanding (MOU) with the BSE and/or NSE. If an RSE entered into such an MOU with the BSE or NSE and the SEBI approved the same, the Trading Members of such RSE would be allowed to trade on the NSE/BSE's trading platform, and shares of companies which were exclusively listed on such RSE (which did not have a trading platform of its own or whose trading platform had become non-operational) could be traded through the trading platform of the BSE or NSE as the case may be. This enabled RSEs to once again become active Stock Exchanges without having to spend huge sums of money to make their own trading platform operational or create their own trading platform where none existed. The VSEL has also

recently entered into such an MOU with the NSE which has been approved by the SEBI and the bye-laws thereof have also been approved by the SEBI and are awaiting publication in the Official Gazette.

Initially, the membership card bestowed ownership and trading rights upon the Trading Members of the Stock Exchanges. During the period 2000-06, the Stock Exchanges all over the world including India underwent a process of corporatisation (whereby the Stock Exchange would be succeeded by another Stock Exchange which would be a company) and demutualisation (whereby the ownership and management would be segregated to some extent from trading rights). For such purpose, the SCRA was amended in the year 2004 to provide for the Demutualisation and Corporatisation of Stock Exchanges.

The newly inserted Section 4A provided for corporatisation and demutualisation of all recognised Stock Exchanges on and from the appointed date (which the SEBI would appoint). Section 4B provided for submission of a Scheme for Corporatisation and Demutualisation, approval and consequent publication thereof by the SEBI.

At the time of approving the Scheme, the SEBI has certain powers to restrict the voting rights of shareholder Trading Members, the rights of the Shareholders or Trading Members to appoint representative on the Governing Board and the maximum number of representatives of Trading Members (not exceeding one fourth) to be appointed on the Governing Board. Furthermore, notwithstanding anything to the contrary contained in the SCRA or any other law, agreement, award, judgment, decree or instrument, upon publication, the Scheme would become binding on all persons and authorities.

Pursuant to this, in 2005, the VSEL was converted into a company limited by shares and also submitted its Corporatisation and Demutualisation Scheme, 2005 providing, *inter alia*, that 51% shareholding would be of the public. After certain revisions, the said Scheme was approved by the SEBI under Sections 4B(6) and (7) of the SCRA on 15.9.2005.

The Scheme contained several provisions with regard to the shareholding rights, the composition of the Governing Board, etc. Some of the important provisions of the said

Scheme are reproduced hereunder:

4 Governing Board

4.1 The first Governing Board on re-registration shall comprise of Directors as are named as first directors in the Articles of Association of VSEL subject to the condition that the representatives of the Members do not exceed one-fourth of the total strength of the Governing Board.

4.2 The Governing Board, on and from Due Date, shall be constituted in accordance with the provisions of the Articles of Association of VSELin force from time to time:

Provided that -

(i) the representation of Trading Members does not exceed one-fourth of the total strength of the Governing Board, and the remaining directors are appointed in the manner as may be specified by SEBI from time to time, and

(ii) the Chief Executive, by whatever name called, is an ex-officio director.

4.3 Notwithstanding anything contained in clause 4.3, SEBI may nominate directors on the Governing Board as and when deemed fit.

6. Demutualisation

6.1 A Trading Member may or may not be a Shareholder.

6.2 A Shareholder may or may not be a Trading Member.

8. Shareholding Rights

8.1 VSEL shall ensure that at least 51% of its equity shares are held by public other than shareholders having trading rights in the manner and within the period prescribed in sub-section (8) of section 4B of the SCRA.

8.2 On and from the Appointed Date, VSEL shall ensure that public other than shareholders having trading rights continuously hold at least 51% of equity shares.

8.3 On and from Due Date, no Shareholder, who is a Trading Member of any recognised Stock Exchange, shall have voting rights (taken together with voting rights held by him and by persons acting in concert with him) exceeding 3% of the voting rights in VSEL.

9. Memorandum and Articles of Association, etc

9.1 The Memorandum and Articles of Association, Rules, Bye-laws and Regulations of VSEL on the day preceding the Due Date shall, unless contrary to or inconsistent with or excluded by this Scheme, apply to it on and from the Due Date.

9.2 VSEL shall incorporate the provisions of this Scheme appropriately in its Memorandum and Articles of Association, Rules, Bye-Laws and Regulations on or before the Due Date.

9.3 Memorandum and Articles of Association, Rules, Bye-Laws and Regulations of VSEL may be amended after the Due Date in accordance with the applicable laws, provided that no such amendment is inconsistent with any provision of this Scheme.

12. Compliance with this Scheme

12.1 VSEL shall ensure compliance with the provisions of this Scheme at all times and shall not do anything contrary to the provisions of this Scheme.

12.2 Without prejudice to the generality of the provisions in clause 12.1, VSEL shall continuously comply with the provisions in clauses 4.3, 6, 7.3, 7.4, 7.5, 7.6, 9.2, 8.3, 9.3 and 11.

12.3 VSEL shall report compliance with the provisions of this Scheme in such manner as may be required by SEBI from time to time.

According to the provisions of the Scheme read with Section 4B(8) of the SCRA, within 12 months from the date of publication of the SEBI's order approving the Scheme, the

VSEL was required to ensure that atleast 51% of its equity shares were held by public other than shareholders having trading rights either by fresh issue of shares to the public or by any other means specified by the SEBI. Moreover, on and from the due date, no shareholder, who was also a Trading Member, would have voting rights exceeding 3%. It is clear that the shareholding of Trading Members was required to be reduced to 49% and their voting rights were also curtailed by the SEBI in exercise of its powers under Section 4B(6) of the SCRA. As regards the Governing Board, it was provided that, on and from the due date, the Governing Board would have to be constituted in accordance with the VSEL's Articles of Association and that representation of Trading Members could not exceed one-fourth of the total strength and the remaining Directors would be appointed in the manner specified by the SEBI from time to time. It was also provided that the Chief Executive would have to be an ex-officio Director. Therefore, even as regards the representation of Trading Members on the Governing Board, the SEBI had exercised its powers under Section 4B(6) of the SCRA.

In terms of Clause 3.1 of the Scheme (which provided that the remaining Directors would be appointed in the manner

specified by the SEBI from time to time), the SEBI, thereafter, issued a letter dated 21st September 2005, *inter alia*, specifying the manner of appointment of the remaining Directors of the VSEL. Some of the relevant clauses or extract thereof as per the said letter are reproduced hereunder:

> *1.0: Governing Board of Vadodara Stock Exchange Limited*
>
> *1.1 Board Composition on and from Due Date till Appointed Date.*
>
> *On and from Due Date, as defined in clause 2.1 of Vadodara Stock Exchange (Corporatisation and Demutualisation) Scheme, 2005, composition of Governing Board shall be as under:*
>
> *1.1.1 Trading Member Directors shall constitute maximum of one-fourth of the total strength of the Governing Board.*
>
> *1.1.2 Public Interest Directors shall constitute the balance of the Governing Board.*
>
> *1.2: Board composition on and from Appointed Date*
>
> *On and from Appointed Date, as may be notified by SEBI under Section 4A of the Securities Contracts (Regulation) Act, 1956, the composition of the Governing Board shall be as under:*

1.2.1 Trading Member Directors shall constitute maximum of one-fourth of the total strength of the Governing Board.

1.2.2 Public Interest Directors shall constitute one-fourth of the total strength of the Governing Board.

1.2.3 Shareholder Directors shall constitute the balance of the Governing Board. In case, the Exchange has strategic partner(s)/majority shareholders, at least one third of the Shareholder Directors shall be independent non-executive Directors.

For the purpose of this clause, the term

i) 'Independent Director' shall have same meaning as assigned to it in the Corporate Governance norms specified by SEBI under the Listing Agreement.

ii) 'strategic partner/majority shareholder' shall mean a shareholder who along with persons acting in concert with him holds 15% or more shares or voting rights in the Exchange.

1.3: General requirements

1.3.1 The Directors, except the Chief Executive such as CEO, ED or MD, etc. shall be elected by the

shareholders.

1.3.2 .....

1.3.3 'Trading Member Directors' shall be elected from amongst the Trading Members.

1.3.4 'Shareholder Directors' shall be elected from amongst the persons, who are not Trading Members or Associates of Trading Members.

.....

1.3.5 'Public Interest Directors' shall be elected from amongst the Persons in the SEBI constituted panel. A person shall not act as 'Public Interest Director' on more than one Stock Exchange simultaneously.

1.3.6 The Chairman shall be elected by the Governing Board from amongst the non-executive non-Trading Member directors.

1.3.7 Manner of election, appointment, tenure, resignation, vacation, etc. of Directors (except the Chief Executive) shall be governed by the Companies Act, 1956 save as otherwise specifically provided under or in accordance with the Securities Contracts (Regulation) Act, 1956.

1.3.8 The Chief Executive shall be an ex-officio Director on the Governing Board.

1.3.9 No approval of SEBI shall be required for appointment of any Director except for the Chief Executive.

1.3.10 SEBI may nominate Directors on the Governing Board as and when deemed fit.

2: Chief Executive

The appointment, renewal of appointment and the termination of service of the Chief Executive shall be subject to prior approval of SEBI. .....

Therefore, there was a change to be effected in the Governing Board on and from the Appointed Date, whereby the Trading Members would constitute one fourth, Public Interest Directors would constitute one fourth and Shareholder Directors would constitute the balance. The reason for this change was that, after the Appointed Date, 51% of the equity share capital was required to be held by the public other than shareholders having trading rights. From the aforesaid, it is clear that, even after the Appointed Date, Trading Members were entitled to have a representation on the Governing Board to the extent of one-fourth. It is clear that the SEBI had exercised its powers under Section 4B(6) of the SCRA read with Clause 3.1 of the Scheme.

As could be seen from the provisions of the SCRA, the Scheme and the subsequent letter dated 21st September 2005, at the time of approval of the Scheme and even thereafter, there was no condition imposed that the VSEL (or any Stock Exchange), for getting or retaining its recognition under the SCRA, was required to have a minimum net worth of any prescribed amount or an annual turnover of any particular amount.

Pursuant to this, on 13th November 2006, the SEBI issued the Securities Contracts (Regulation) (Manner of Increasing and Maintaining Public Shareholding in Recognised Stock Exchanges) Regulations, 2006. The said regulations were applicable to all the recognised Stock Exchanges in respect of which the Scheme for corporatisation and demutualisation had been approved by the SEBI and prescribed by the manner in which public shareholding could be increased, which could be done by various means including fresh issue of equity shares to the public through issue of prospectus or issue of shares on private placement basis to persons other than shareholder having trading rights or their associates, subject to the SEBI's approval. The said regulations also provided that no person

could hold more than 5% in the paid up equity capital of a recognised Stock Exchange and that no person could either individually or together with persons acting in concert with him acquire and/or hold more than 1% of the paid up equity share capital of a recognised Stock Exchange unless he is a fit and proper person and has taken prior approval of the SEBI.

In the backdrop of the aforesaid existing conditions/stipulations, since it was necessary to ensure that, within the stipulated period, 51% of the equity share capital was held by the public other than shareholders having trading rights, the VSEL decided to go for the issue of shares on private placement basis and, therefore, issued an Information Memorandum for Inviting Expression of Interest. Pursuant to this, by issuing 51% of its equity shares to the public, the VSEL has complied with the said condition. Thereafter, the Governing Board of the VSEL consisted of 3 Trading Member Directors, 3 Public Interest Directors and 6 Shareholder Directors (including the Chairman). Therefore, the VSEL was fully complying with the requirements of the Scheme and the SEBI's direction under Section 4B(6) of the SCRA.

On 29th December 2008, the SEBI issued another circular

which gave guidelines to provide an exit option to such RSEs whose recognition had been withdrawn or was under renewal or had been refused by the SEBI or those who wanted to surrender their recognition. The guidelines dealt with the issue of retention of assets by such RSE on fulfillment of certain conditions and also provided that, upon derecognition, the Stock Exchange would continue to be a corporate entity under the Companies Act, 1956, and its subsidiaries could continue to function as a normal broking entity and the Trading Members thereof would be deregistered. It further provided, *inter alia*, that companies listed with a derecognised RSE and also listed with another Stock Exchange would continue to be listed in such other Stock Exchange whereas companies listed exclusively on the derecognised RSE would have to either seek listing at another Stock Exchange or provide exit option to shareholders as per SEBI Delisting Guideline.

According to the requirements of law, the SEBI directed the corporatisation and demutualisation of several Stock Exchanges, including the VSEL, during the period 2004 to 2007 and asked them to go ahead and invite various investors to purchase a total of 51% equity shares, thereby causing innocent persons to invest their monies for purchasing shares

in Stock Exchange under the belief that such recognised Corporatised and Demutualised Stock Exchanges, having complied with all the requirements of law, would continue to be recognised and be allowed to carry on their business unhindered by any constraints/conditions (other than those already existing at the time of corporatisation and demutualisation).

In the year 2010, the SEBI constituted a committee under the Chairmanship of Dr.Bimal Jalan, Former Governor of the Reserve Bank of India. Although the provisions regarding ownership structure and board composition of Stock Exchanges, listing of Stock Exchanges, etc. had already been provided for in the SCRA and the approved Schemes of Corporatisation and Demutualisation, including the Scheme, yet the terms of reference of the Committee included reviewing and make recommendations on the said aspects. The Committee gave its report on 22nd November 2010, making several recommendations which would not only be contrary to the SCRA and the Companies Act, 1956, but would also affect the fundamental and legal rights of the Stock Exchanges, their Trading Members, investors and listed companies.

After a period of more than 7 years since the approval of the Scheme, the SEBI has recently issued a Circular dated 30th May 2012, modifying the earlier Circular dated 29th August 2008 and, *inter alia*, containing the following provisions:

2. Process of Derecognition and Exit

2.1 ....

2.2: Stock Exchanges where the annual turnover on its own platform is less than Rs. 1000 crore can apply to SEBI for voluntary surrender of recognition and exit at any time before the expiry of two years from the date of issuance of this circular.

2.3: If the Stock Exchange is not able to achieve the prescribed turnover of Rs. 1000 crores on continuous basis or does not apply for voluntary surrender of recognition and exit before the expiry of two years from the date of this Circular, SEBI shall proceed with compulsory derecognition and exit of such Stock Exchanges, in terms of the conditions as may be specified by SEBI.

Therefore, after having demutualised the Stock Exchanges and having allowed the public to invest in 51% of the shares of Stock Exchanges, the SEBI has now stipulated a further condition of achieving a turnover of Rs.1000 crore on a

continuous basis, that too on their own platform, failing which the SEBI would proceed to derecognise such Stock Exchanges.

The Circular further provides that, in case of such derecognition and exit, exclusively listed companies would be required to apply for listing in another Stock Exchange and, if they fail to obtain such listing, they would cease to be a listed company and would be moved to the Dissemination Board where the willing buyers and sellers of securities of such companies would be given an opportunity to disseminate. The Circular also provides that such derecognised Stock Exchanges may provide opportunity to their Trading Members to trade on Stock Exchange having nationwide terminal through their subsidiary company which will function as a normal broking entity. The Circular also contains provisions with regard to treatment of assets of derecognised Stock Exchanges including provisions to the effect that valuation would be done by the SEBI appointed agency, up to 20% of the assets post tax would have to be contributed towards the SEBI Investor Protection and Education Fund, that dues of brokers would have to be paid by such Stock Exchange and also that such Stock Exchanges cannot alienate any assets without taking prior approval of the SEBI. The Circular appears to have been issued

in exercise of purported powers under Section 11 of the SEBI Act and Section 5 of the SCRA.

Thereafter, in purported exercise of powers under Sections 4, 8A and 31 of the SCRA read with Sections 11 and 30 of the SEBI Act, on 20th June 2012, the SEBI has issued the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012.

By way of the Regulations, the composition of the Governing Board was sought to be altered contrary to the provisions of the Scheme and the time period for this to be done was only three months. Hence, as on 20th September 2012, the composition of the Governing Board of the VSEL was altered by removing all the three Trading Members from the Governing Board and, out of the total strength of 12 posts (excluding Managing Director), 6 posts were reserved for Public Interest Directors and 6 posts were reserved for Shareholder Directors. Sometime thereafter, the Governing Board of the VSEL consisted of only 1 Public Interest Director and 3 Shareholder Directors and the rest of the posts were vacant.

On 28th November 2012, the Governing Board of the VSEL issued a notice calling an Extra Ordinary General Meeting of the shareholders of the VSEL to be held on 29th December 2012. According to the said notice, the business to be transacted therein is the appointment of 4 Directors in the category of "Shareholder Director". The said notice is completely contrary to the Scheme and the Companies Act, 1956. Moreover, in view of the Regulations, Trading Members of the VSEL who are also shareholders will not be permitted to vote in the election of the 4 persons who are to be appointed as Shareholder Directors.

Thereafter, the SEBI issued another Circular No. CIR/MRD/DSA/33/2012 dated 13th December 2012, *inter alia*, stipulating that every recognised Stock Exchange having net worth less than Rs.100 crore as on the date of commencement of the Regulations would be required to submit its plan to the SEBI for achieving the net worth in terms of the Regulations within 90 days from the date of the Circular dated 13th December 2012.

In such circumstances referred to above, the petitioners have prayed for the following reliefs :

"A. This Hon'ble Court be pleased to issue a writ of or in the nature of mandamus or any other appropriate writ, order or direction holding and declaring that the Circular dated 30.5.2012 at ***Annexure H*** *hereto, the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 at* ***Annexure I*** *hereto, the notice dated 28.11.2012 issued by VSEL at* ***Annexure J*** *hereto and the Circular dated 13.12.2012 at* ***Annexure K*** *hereto are ultra vires the Constitution of India, the Securities Contracts (Regulations) Act, 1956 and are in contravention of the Companies Act, 1956 and are unreasonable, unconstitutional, discriminatory, inequitable, unjust, harsh and illegal.*

B. This Hon'ble Court be pleased to issue a writ of or in the nature of mandamus or any other appropriate writ, order or direction holding and declaring that the provisions of the schemes for corporatisation and demutualisation, which are approved by SEBI and are published as per the requirements of Section 4B of the Securities Contracts (Regulation) Act, 1956, have full effect and are binding.

C. Pending the admission, hearing and final disposal of the present petition, this Hon'ble Court be pleased to stay and suspend the operation and implementation of the Circular dated 30.5.2012 at ***Annexure H*** *hereto, the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 at* ***Annexure I***

hereto, the notice dated 28.11.2012 at ***Annexure J*** *hereto and the Circular dated 13.12.2012 at* ***Annexure K*** *hereto.*

D. Pending the admission, hearing and final disposal of the present petition, this Hon'ble Court be pleased to restrain the respondent no. 3 herein from taking any steps in furtherance of the notice dated 28.11.2012 at ***Annexure J*** *hereto.*

E. Ex parte ad interim reliefs in terms of prayers C and D hereinabove be granted.

F. Such other and further reliefs as deemed just and expedient be granted."

I. Stance of the respondent no.2 SEBI

(A) Preliminary objections raised on behalf of the respondent no.2 as regards the maintainability of the writ-petition :

(1) The petitioners claiming to be the Trading Members and shareholders of the VSEL have filed the petitions on the premise that their fundamental right as enshrined under Article 19(1)(g) of the Constitution of India has been violated and such violation is the foundation for

invoking the jurisdiction of the High Court under Article 226 of the Constitution of India. The rights that can be enforced under Article 226 of the Constitution of India ordinarily must be the rights of the petitioners as an individual except in cases of habeas corpus, quo warranto and public interest litigation. The petition of the present nature is not maintainable and none of the fundamental rights or any other legal rights of the petitioners could be said to have been infringed by issuance of the impugned circulars.

(2) The petition mainly highlights the problems caused for the Stock Exchanges on account of the impugned regulations and circulars. The Stock Exchange is not the petitioner before the Court nor it has any grievance with the impugned regulations and circulars. The petitioners who are indisputably the Trading Members are not being divested of their right to trade as the SEBI had permitted the VSEL to form a subsidiary stock broking firm, which is a member of the other national exchanges. Therefore, the petition is not maintainable.

(3) The SEBI, *vide* circular dated 26th November 1999,

permitted the small Stock Exchanges to promote/float a subsidiary company to acquire the membership rights of the other Stock Exchanges. Such a measure was introduced after considering the suggestions/revival plans forwarded by the small exchanges for their revival. The petitioners function as sub-brokers also and have been granted a certificate of registration by the SEBI. The livelihood of the petitioners is not affected in any manner on account of the conditions imposed on the Stock Exchanges by the SEBI for their proper functioning.

(4) The communication from the VSEL and the shareholders including the Trading Member shareholders of the VSEL clearly reveals that the object behind filing the instant writ-petition is that, while the majority of the shareholders of the VSEL desired to seek derecognition, the Stock Exchange has opposed to the desire of the Trading Member shareholders of the Stock Exchange. As the Trading Member shareholders are unable to convince the majority of the public shareholders, this petition has been filed challenging the policy decision of the SEBI.

(5) The total number of Trading Members of the VSEL

are 289. The petition has been filed only by 52 persons holding 405812 shares of the VSEL, which constitute 7% of the total share capital of the Stock Exchange.

(6) As the petition has not been filed by the Stock Exchange nor the Stock Exchange has lodged their objections to the provisions of the new regulation and the exit circular, this petition is not maintainable as it is intended to serve the interest of few Trading Member shareholders of the VSEL, i.e. 7% of the Trading Members only.

(7) The appropriate forum for redressing the grievance would be the Company Law Board and not by filing a writ-petition invoking the writ jurisdiction of the High Court under Article 226 of the Constitution of India.

(8) The SEBI has introduced the policy to serve the interests of the stakeholders concerned and is done more in public interest. A handful of Trading Members of a Stock Exchange (i.e. 7%), if are aggrieved by the policy formulated in public interest, then the same cannot be modified only with a view to benefit 7% of the Trading

Members of a Stock Exchange.

(9) Out of 23 recognized Stock Exchanges, only 3 Stock Exchanges which include the VSEL, have not put forward any plan for revival or any indication to exit. Three Stock Exchanges have already exited from the business of Stock Exchange, viz. HSE, SKSE, Coimbatore Stock Exchange, and eight Stock Exchanges have applied voluntarily to be derecognized as Stock Exchanges. None of the Stock Exchanges have challenged the provisions of the impugned regulations or circulars.

(10) The VSEL is in a pathetic condition. There has been no trading in the VSEL since April 30, 2003. According to the SEBI circular dated 7th October 2009, the Stock Exchanges which are defunct or have been inactive for more than six months are required to seek the approval of the SEBI before commencing with the trade. Such approval is granted after conducting the necessary inspection of the concerned Stock Exchange. This is to ensure that the systems are running effectively in the Stock Exchange and there is no potential risk to the investors using the terminal of such Stock Exchanges.

The VSEL has not sought any approval from the SEBI for trading past couple of years. However, the renewal of recognition has been sought by the exchange time to time and has been granted by the SEBI. Although there appears to be some interest to continue recognition of the Stock Exchange, yet there does not appear to be any bonafide intention on the part of the Stock Exchange or its Trading Member shareholders to initiate and promote trading on the terminal of the VSEL. In such circumstances, the assertion on the part of the petitioners that their fundamental right to carry on any occupation, trade or business is without any substance.

(11) The Saurashtra and Kutch Stock Exchange (SKSE) had filed an appeal challenging the order passed by the SEBI withdrawing the recognition and the same was ordered to be dismissed by the Securities Appellate Tribunal *vide* order dated 13th July 2007 mainly on the ground that the SKSE remained defunct for almost nine years. The decision of the Tribunal was affirmed by the Supreme Court.

(12) The continued existence of defunct exchanges and

those which are not properly managed may prove to be detrimental to the safety of the securities market as such exchanges could be used as a platform to conduct manipulation practices in the securities market.

II. Overall stance of the SEBI :

The SEBI has been established under the Securities and Exchange Board of India Act, 1992 as a statutory and regulatory body to protect the interest of the investors in securities and to promote the development of, and to regulate the securities market and for matters connected therewith or incidental thereto. The SEBI is an expert body in the securities market.

Under Section 11(2)(a) of the SEBI Act, it has authority to regulate business in Stock Exchanges and other securities market. Further, in terms of Section 11(2)(j) of the SEBI Act, it performs such functions and exercise such powers under the provisions of the Securities Contracts (Regulation) Act, 1956 as may be delegated to it by the Central Government.

The object of the SCRA is to prevent undesirable transactions in securities by regulating business of dealing

therein and by providing for certain other matters connected therewith. That Section 29A of the Securities Contracts (Regulation) Act, 1956 provides for delegation of powers to be exercisable by the Central Government to the SEBI by an order of the Central Government, in relation to such matters and subject to such conditions as may be specified in the order. In terms of the Notification dated 13th September 1994, the SEBI was invested with power to grant/withdraw recognition to a Stock Exchange including the power exercisable under following provisions of the SCRA:

Section	**Nature of Power**
3	Application for recognition of Stock Exchange
4(1)	Grant of recognition to Stock Exchange
4(2)	Conditions for grant of recognition of Official Gazette
4(3)	Publication of grant of recognition in Official gazette
4(4)	Refusal of recognition to be communicated
5	Withdrawal of recognition to Stock Exchange
7A(2)	Approval of rules restricting voting rights, etc.
13	Contracts in notified areas illegal
18(2)	Applicability of provisions of section 17 to spot delivery contracts
22	Right of appeal to SEBI against such refusal,

omission or failure

28(2) SCR Act not to apply to any class of contracts

Thus, the SEBI exercises powers concurrently with the Central Government under the SCRA.

In addition to the aforesaid delegated powers, the SEBI has also been conferred powers directly by the Parliament under the provisions of the SCRA which include the power-

(a) to approve and notify the Scheme in respect of Corporatisation and Demutualisation of a Stock Exchange, (Section 4A, Section 4B);

(b) to approve the transfer of the functions of a clearing house to a clearing corporation and to approve the bye-laws of clearing corporation, (Section 8A);

(c) to issue directions to the Stock Exchange, clearing corporation and any person associated with the securities market,(Section 12A);

(d) to adjudicate and impose monetary penalty (Section 23A to 23J); and to frame regulation for carrying out the purposes of the Act (Section 31).

A Stock Exchange is constituted for the purposes of assisting, regulating and controlling the business of buying, selling or dealing in securities. Thus, it has to ensure that the business in Stock Exchange is conducted in a fair manner and in the interests of investors and the securities market. It is a first level regulator which regulates and controls the contract in securities entered at the Stock Exchange and thus it works in the interests of the investors and the securities market and performs functions for the benefit of public/investors and thus performs a public duty.

The Stock Exchanges are considered as Infrastructure Institutions for Securities Market of a country. This is because financial institutions like Stock Exchanges are central to the national economy and at the core; there would be the issue of safety of the wealth of the citizens who avail the services they offer. Therefore, for the economic health of the country which encompasses public good also, it is of utmost importance that Stock Exchanges perform their functions in a manner which contributes to economic benefit of the Country. For this purpose, their sound financial health, good management and ownership and substantial business activities are foremost. All these aspects are taken care of in the provisions of the SEBI

Act, the SCRA, the Rules and Regulations framed thereunder including the directives issued by the SEBI from time to time.

The Central Government announced its proposal to corporatize and demutualise the Stock Exchanges by which, *inter alia*, ownership, management and trading rights would be segregated from each other. Accordingly, the SEBI constituted a group headed by Justice M.H.Kania, Hon'ble the then Chief Justice of India, on Corporatisation & Demutualisation of Stock Exchanges in India. The group submitted its report on August 28, 2002. Subsequently, Sections 4A and 4B were inserted in the SCRA *vide* Securities Laws (Amendment) Act, 2004, (w.e.f. 12th October 2004). Sections 4A and 4B of the SCRA enabled the SEBI to put into place a mechanism of separation of ownership and control of Stock Exchanges from Trading Members by implementing a Scheme for Corporatization and Demutualisation. Conflicts of interest of Trading Members were sought to be obviated by ensuring a disassociation between members who trade on the exchange and control over the ownership of the exchange. Further, every recognised Stock Exchange, in respect of which the Scheme for Corporatization or Demutualisation had been approved was mandated to ensure that at least fifty-one per cent of its equity share capital

is held by the public other than shareholders having trading rights, in accordance with the regulations made by the SEBI. For this purpose, the SEBI notified SC(R) (Manner of Increasing and Maintaining Public Shareholding in Recognized Stock Exchanges) Regulations, 2006 (hereinafter referred to as 'MIMPS Regulations') which were subsequently repealed by the impugned regulations.

Although after corporatisation and demutualisation of Stock Exchanges, a Stock Exchange is a company incorporated under the Companies Act, 1956, yet its constitution and management and functions are regulated by the provisions of the SCRA. The SCRA being the special enactment prevails over other Acts including the Companies Act, in respect of the regulation of Stock Exchanges. Specifically, certain provisions of the SCRA have been given explicit over riding effect over the Companies Act or any other law for the time being in force. Such provisions include power to make rules including the rules restricting voting rights of members, providing restriction on the right of a member to appoint proxy, providing regulation of voting rights so that each member may be entitled to have only one vote irrespective of his share in the paid up equity capital in the Stock Exchange (Section 8

read with Section 7A); power to restrict the representation of the stock broker on the governing board {Section 4B(6)}; power to restrict the right of shareholders to appoint the representatives on the governing board, {Section 4B(6)}; the manner in which at least 51% of equity share capital of a recognized Stock Exchange is held by the public other than the shareholder having trading rights Section 4B(8)}; and power of SEBI to make rules relating, *inter alia,* to the governing body of the Stock Exchange, its constitution and powers of management, duties of office bearers of the Stock Exchange, etc (Section 8 read with section 3).

Under Section 11 of the SCRA, the Central Government/SEBI may supersede the governing board of a Stock Exchange. This power is conferred with the objective to provide a mechanism of regulation of business and prevention of undesirable transactions in securities in the Stock Exchange and to ensure that its functioning does not adversely affect the interest of the investors, securities market and further to ensure the compliance of the provisions of the SCRA, the SEBI Act or rules and regulations framed thereunder or directives issued thereunder.

The powers exercisable by Central Government under

SCRA are also exercisable by the SEBI by virtue of general delegation made by the Central Government in favour of the SEBI. Earlier, the Central Government had framed the Securities Contracts (Regulation) Rules, 1957 (hereinafter known as 'SCRR'), however, the administration and enforcement of the SCRR lies with the SEBI.

After the demutualization process Stock Exchanges had become for-profit companies and were free to pursue their economic interest objectives, which was in conflict with their role as a first level regulator. Therefore, there was a need to formulate a regulatory policy to resolve the conflict of interest issues and to have a balance between profit making objective of a Stock Exchange versus its regulatory role, conflict between the profit making entity versus its place in security market as a public utility. Therefore, the SEBI appointed an expert committee under the Chairmanship of Dr.Bimal Jalan, Ex-Governor, Reserve Bank of India, to examine issues arising from the ownership and governance of Market Infrastructure Institutions viz. Stock Exchanges, Clearing Corporations and Depositories. The said committee submitted its report to the SEBI on 22nd November 2010, after following consultative approach.

The respondent No.3 had given its comments on the said report. The Federation of Indian Stock Exchanges (FISE) of which respondent No.3 is also a member, had also given its comments on the said report.

The recommendation of the Jalan Committee and the public comments received thereon and issues regarding exit of de-recognised/non-operational Stock Exchanges were discussed in the meeting of the SEBI Board held on 2nd April 2012. The SEBI Board has representatives from MoF, MCA, RBI, etc. After deliberations, the Board took the decisions regarding ownership and governance norms for market infrastructure institutions. These decisions so far as they related to recognition, de-recognition, ownership and management of Stock Exchanges and clearing corporation were implemented through Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012, to provide for the ownership and governance norms for Stock Exchanges and clearing corporations. Based on the policy approved by the Board regarding voluntary/compulsory derecognition and exit of Stock Exchanges including de-recognised Stock Exchanges, circular dated 30th May 2012 was issued.

The impugned regulations have been framed by the SEBI in exercise of the powers conferred by Sections 4, 8A, and 31 of the SCRA read with Sections 11 and 30 of the SEBI Act. As stated above in terms of Section 11 of the SEBI Act, the SEBI has been entrusted with the task of protection of investors and development of securities market. Scope and objective of the said section has been extensively dealt with by the Hon'ble Supreme Court in its recent judgments, and the Hon'ble Supreme Court has held that under the said section the SEBI has wide powers to protect the interest of investors and for the development of securities market. Under Section 12-A of the SCRA, the SEBI also has powers to issue directions to Stock Exchanges, listed companies and other persons associated with the securities market, *inter alia,* in the interest of investors or orderly development of securities market, to prevent the affairs of any recognized Stock Exchange or clearing corporation from being conducted in a manner detrimental to the interests of investors or securities market; and to secure proper management of such Stock Exchange or clearing corporation or any other persons providing trading or clearing or settlement facility in respect of securities.

The impugned regulations retain the principles of SC(R)

(MIMPS) Regulations, 2006 (since repealed) which prescribed the ownership norms for Stock Exchanges. The impugned regulations, additionally prescribes entry/eligibility norms, ownership structure and governance norms, etc for Stock Exchanges and clearing corporations. One of the major requirements which were imposed under these regulations was that the board of Stock Exchanges and clearing corporations shall not have Trading Member/clearing member representation and their associates and agents and shall consist only of Public Interest Directors and shareholder directors.

The norms restricting the appointment of Trading Members on the board of Stock Exchange was based upon the reasons that the Trading Members on the board of Stock Exchange are privy to confidential information and have a conflict of interest in respect of the following issues:

a) Companies listed on Stock Exchanges are required to make various disclosures to Stock Exchanges in terms of listing agreement entered with Stock Exchanges. These disclosures contain price sensitive information having potential to influence

the price of the shares of the company, which may not be available to general public at large, at that time. The presence of Trading Members on the board of Stock Exchanges who trades in securities has the effect of compromising the confidentiality of such information;

b) The Stock Exchange being first level regulator undertakes real time surveillance of trading in the market. In this process the board of the Stock Exchanges comes in the possession of price sensitive information and Trading Members on the board may use this information to their advantage.

c) The Stock Exchange being first level regulator also undertakes risk management functions and it has to ensure level playing field to all the market participants. However, Trading Members by virtue of their position as board members may take decisions regarding risk management to their advantage which may compromise the risk management thereby imperiling the integrity of the securities market.

d) In terms of section 9 of the SCRA the Stock Exchanges are inter alia empowered to make bye laws which may provide for imposition of penalties and fines on its members. The presence of Trading Members on the board of Stock Exchanges will have inherent conflict in this regard.

e) Some of the real incidents of conflict which has damaged the integrity of the securities market are highlighted below:

In the year 2001, the President of the Bombay Stock Exchange who was also a Trading Member had illegally obtained some price/market sensitive information, from an officer of the surveillance department in the presence of certain other brokers. During the investigation the transcripts of telephonic conversation revealed that the President had obtained information in respect of certain specific scrips and brokers. In this regard SEBI restrained the President from acting as a Director Member of the Governing Board of the Stock Exchange, Mumbai. The said SEBI order was upheld by the Hon’ble Bombay High Court in Anand Rathi and Ors. v.

SEBI, 2002 (2) Bom CR 403;

In the year 2001, a settlement crisis arose in the Calcutta Stock Exchange, wherein the Trading Members were also involved in the management of the Stock Exchange. In this regard, Joint Parliamentary Committee, 2001 which conducted investigation into the said crisis had brought out in detail the reasons for the crisis in Chapter VI of the Report. The Report had, *inter alia*, brought out that CSE could have prevented the "payment crisis" by strictly following the SEBI directives on margins and exposure limits. Further the report also brought out the following deficiencies :

- Deficiencies in Surveillance
- Deficiencies in Risk Management System
- Violation of exposure limits
- Delay in deactivating terminals
- Delayed action on dishonoured cheques of margin payment

-
- Conflict of Interest in respect of the elected board members of the exchange were interfering in the day-to-day matters of the exchange.

However, the SEBI Board, giving due regard to the need of operational and commercial expertise of Trading Members, in the impugned regulations, a concept of Advisory Committee

(comprising only of Trading Members and the Managing Director) has been introduced whose task will be to advise the Board of Stock Exchange on the non-regulatory and operational matters including product design, technology, charges and levies. Advisory Committee has been mandated to have at least four meetings in a year with not more than three months gap between two meetings. Further, impugned regulations mandate that the recommendations of the Advisory Committee shall be placed in the ensuing meeting of the Governing Board of the recognized Stock Exchange for consideration and appropriate decision of the Governing Board, and such recommendations along with the decision of the Governing Board on the same, shall be disclosed on the websites of the Stock Exchange. Thus, the impugned tegulations ensure that the Trading Members continued to be involved in the operational and non-regulatory matters as elaborated above.

The Stock Exchange as an institution is central to the securities market facilitating the business of buying and selling or dealing in securities, wherein the market participants transact their business with the participation of investors, brokers and sub-brokers etc. A Stock Exchange in India is

recognized by the SEBI under Section 4 of the Securities Contracts (Regulation) Act, 1956, for the aforesaid purposes and over a period of time the Stock Exchanges were setup almost in every State to provide a centre in the region and were known as Regional Stock Exchanges. These Stock Exchanges were established to enable regional companies in the respective geographical locations to raise capital and to provide an opportunity to the investors to participate in the securities market. However, with the various technological advances in the securities market, the scope of operations of the Regional Stock Exchanges became limited, investors preference for using the platform of such regional Stock Exchanges reduced, and the trading in these smaller Stock Exchanges came down sharply and reduced in the case of most exchanges including VSE to nil in the past few years. The entities transact their business in their Stock Exchanges including the investors have been effected adversely as they do not have the opportunity to transact in the securities market.

The SEBI, in recent past, has withdrawn the recognition granted to the Hyderabad Stock Exchange and Saurashtra Kutch Stock Exchange Ltd., while it has refused renewal of

recognition to Mangalore Stock Exchange, Magadh Stock Exchange Ltd. There are 21 recognized Stock Exchanges in the country and excepting NSE and BSE which account for almost 100% of the total turnover in the equity and equity F & O Segment, only Calcutta Stock Exchange has a trading operations while the business in all other smaller Stock Exchanges is nil.

The first among the initiatives for the revival of the Regional Stock Exchanges was the setting up of the Inter Connected Stock Exchange (ISE) to regroup the Regional Stock Exchanges to provide a third national market. The ISE was promoted in 1998 by 12 smaller Stock Exchanges for providing an additional trading platform where the shares listed on any of these 12 exchanges could be traded. Lack of interest on the part of investors in using the platform of the exchange resulted in lack of liquidity and consequently ICSE did not perform well. Since 2003-04, there is no trading on ICSE. The smaller Stock Exchanges were permitted to set up broking subsidiaries and obtain membership of the BSE and NSE to have access to the markets of BSE and NSE. The establishment of subsidiary broking entities were allowed to aid the Trading Members of the smaller Stock Exchanges for their benefit. In spite of the

aforementioned efforts, the scope of the smaller Stock Exchanges became limited till they virtually lost their relevance, with the advent of modern telecommunication and information technology and the symbiotic interaction of technology and the markets, which facilitated a fundamental transformation of the market micro structure. Smaller Stock Exchanges took up ancillary activities such as training, investor education and depository participant services. The income generated from listing fees and the ancillary activities, return on the investments made by the smaller Stock Exchanges and surplus generated by the subsidiaries became the main sources of revenue for the smaller Stock Exchanges. In conclusion, most of the Smaller Stock Exchanges ceased to be markets where securities of companies listed on them are bought and sold. In fact the obligation, role of the smaller Stock Exchanges to provide trading venues to investors of companies listed on them is lost. These smaller Stock Exchanges are not serving the purpose for which they have been granted recognition thus serving no economic/public purpose.

Steps were taken to revive the Regional Stock Exchanges. The financial condition of the smaller Stock

Exchanges is weak. This state of affairs has been prevailing for the past several years. Some of the factors responsible for the smaller Stock Exchanges not having trading operations are –

a. the advent of automated trading and extension of nationwide reach of BSE and NSE which offered a large and liquid market to investors across the country;

b. the introduction of uniform rolling settlement from June 2001 in place of account period settlement with varying settlement cycles;

c. the abolition of the concept of regional listing; and

d. the liquidity being limited to National Stock Exchanges like NSE and BSE.

e. fair and transparent price discovery with large number of companies being listed.

f. better redressal mechanism in the other Stock Exchanges.

g. preference of investors

Considering the aforesaid facts and to secure interest of the investors in the market, the SEBI, from time to time and

wherever required, appointed expert's committee to examine the important aspects of the securities market and to recommend actions in a specific areas in the interest of the market as well as investors. As stated above the Stock Exchanges are centre institutions to the securities market. Its stability, financial health and continued sustainability are of vital importance to the safety and integrity of the securities market. Hence, it would be reasonable to stipulate that only those entities with substantial financial health and net worth and other specified criteria should be permitted to be Stock Exchanges. One of the parameters used by the SEBI is the criteria of net worth requirement for registration of various classes of intermediaries. The depositories, the depository participants, merchants banks and other various intermediaries registered by the SEBI are required to comply with capital adequacy net worth specified by the SEBI.

The Depositories Act, 1996, prescribes a net worth requirement of Rs.100 crore for depositories. Further, in the year 2008, the RBI-SEBI Standing Technical Committee while laying down the procedures for Exchange Traded currency futures prescribed net worth requirement of at least 100 crore rupees as an eligibility criteria for setting up of currency future

segment in a recognized Stock Exchange. Further, in the year 2009, the SEBI Board decided that a new exchange shall have net worth of at least Rs.100 crores. Taking it forward, the SEBI Board, in its meeting held on 2nd April 2012, decided to prescribe the net worth requirement of Rs.100 crore which will be applicable to Stock Exchanges and Clearing Corporations, by way of impugned regulations. However, looking at the situation of the existing Stock Exchanges, they were allowed three years time to achieve the same.

The Bimal Jalan Committee also observed that MII (including Stock Exchanges) should be a well-capitalized entity so that the net worth of the MII is available as a last resort to meet exigencies and ensure that it is able to remain as a going concern. In view of the above, the impugned regulations prescribed Rs.100 crore net worth criteria, whereas the functional exchanges already had a higher net worth as follows:

- NSE- Rs. 3,316 Crores
- BSE- Rs. 1463.2
- MCXSX -Rs. 240.39 Crores

(Details of net worth as on 31st March 2012)

The trading at smaller Stock Exchanges have declined

and has come to almost nil. Trading on the platform of the Vadodara Stock Exchange is nil since 2003-04. Currently, out of the 17 small/regional exchanges, trading occurs only at the Calcutta Stock Exchange. These Stock Exchanges can be termed as defunct Stock Exchanges for lack of sustainable operations and the shareholders of companies listed on these Stock Exchanges do not have exit option as these companies do not have listing on Stock Exchanges having nationwide trading terminal.

The continued existence of defunct Stock Exchanges requires the SEBI to carry out various regulatory, supervisory and administrative activities which are unproductive and is a regulatory burden. This would have an adverse impact on the interest of investors as well. Consequently, and also based on recommendations of the Ministry of Finance, an exit policy for Stock Exchanges was formulated and brought into effect *vide* the SEBI Circular dated December 29, 2008. The new Circular dated May 30, 2012 is under review of the earlier circular of 2008. The Exit Circular issued by the SEBI on May 30, 2012 was issued after deliberation of the matter in the Secondary Markets Advisory Committee (SMAC). One of the members of the SMAC is the FISE i.e. Federation of Indian Stock Exchanges

which has many Stock Exchanges including respondent no.2, as its members. The FISE had also given its detailed comments on the said policy, as a member of the SMAC. Therefore, even the policy relating to the Exit Circular had been finalized after consultation with the concerned market participants, though the SEBI is not statutorily mandated to undertake prior consultation. The Exit Circular issued by the SEBI on May 30, 2012 deals with the following aspects viz., voluntary surrender of recognition, compulsory de-recognition, companies exclusively listed on the de-recognized Stock Exchanges, Trading Members of de-recognized Stock Exchanges and treatment of assets of de-recognized Stock Exchanges. The annual trading turnover requirement for Stock Exchanges as imposed by the Exit Circular, is by virtue of the powers of de-recognition of Stock Exchanges, given to the SEBI in terms of Section 5 of the SCRA. Section 5 of the SCRA reads:- "If the Central Government is of the opinion that the recognition granted to a Stock Exchange under the provisions of this Act should, in the interest of the trade or in the public interest, be withdrawn, the Central Government may serve on the Governing Body of the Stock Exchange a written notice that the Central Government is considering the withdrawal of the recognition for the reasons stated in the notice, and after

giving an opportunity to the governing body to be heard in the matter, the Central Government may withdraw, by notification in the Official Gazette, the recognition granted to the Stock Exchange."

Exchange-wise Cash Segment Turnover			
Stock Exchange	**2008-09**	**2009-10**	**2010-11**
BSE	11,00,074	13,78,809	11,05,027
NSE	27,52,023	41,38,023	35,77,410
UPSE	89	25	0.12
Calcutta	393	1,612	2,597
Ahmedabad	Nil	Nil	Nil
Bangalore	Nil	Nil	Nil
Bhubaneswar	Nil	Nil	Nil
Cochin	Nil	Nil	Nil
Coimbatore	Nil	Nil	Nil
Delhi	Nil	Nil	Nil
Gauhati	Nil	Nil	Nil
ISE	Nil	Nil	Nil
Jaipur	Nil	Nil	Nil
Ludhiana	Nil	Nil	Nil
Madras	Nil	Nil	Nil
MPSE	Nil	Nil	Nil
OTCEI	Nil	Nil	Nil
Pune	Nil	Nil	Nil
Vadodara	Nil	Nil	Nil
Total	38,52,579	55,18,469	46,85,034

The amount of trading turnover required i.e. 1000 crore, is in itself a very small figure when compared to the total trading turnover in the country on an annual basis. If a Stock Exchange is not able to satisfy even this minimum amount, it

may be inferred that investors are not interested in using the platform of such an exchange to deal in securities. The continued existence of such exchanges would be detrimental to the health and safety of the securities market. The trading volumes (equity and equity F & O) on all the Stock Exchanges during the last three years is as follows:

Trading Turnover details (Amount in Rs. Crore)

Name of the Exchange	**2009-10**	**2010-11**	**2011-12**
BSE	13,78,809	11,05,027	6,67,498
NSE	41,38,023	35,77,410	28,10,892
CSE	1,612	2,597	5,991
VSE	NIL	NIL	NIL

The smaller 16 Stock Exchanges including VSEL do not have any trading/turnover. It may be noted that out of 21 recognized Stock Exchanges, two i.e. MCX-SX and USEIL presently have trading in Currency Derivatives segment. From the above table it can be seen that the condition of Rs 1000 crore turnover prescribed is minuscule compared to the trading volumes on the other exchanges. Moreover, a time period of two years has been given to achieve the prescribed turnover of Rs. 1000 crore. Also it can be seen from the above

table that the VSEL trading turnover has dwindled and come to nil since 2003-04. The following table indicates the period from which there has been no trading activity on non-operational Stock Exchanges:

Sr. No.	**Name of the Stock Exchange**	**No trading since**
1	Ahmedabad Stock Exchange	2004-05
2	Bangalore Stock Exchange	2002-03
3	Bhubaneswar Stock Exchange	2000-01
4	Cochin Stock Exchange	2002-03
5	Coimbatore Stock Exchange	2000-01
6	Delhi Stock Exchange	2004-05
7	Gauhati Stock Exchange	1999-00
8	Inter-connected Stock Exchange	2003-04
9	Jaipur Stock Exchange	2000-01
10	Ludhiana Stock Exchange	2002-03
11	Madhya Pradesh Stock Exchange	2002-03
12	Madras Stock Exchange	2007-08
13	OTCEI	2004-05
14	Pune Stock Exchange	2003-04
15	Uttar Pradesh Stock Exchange	2010-11
16	Vadodara	2003-04

The impugned circular prescribes that the Stock Exchanges if they are unable to achieve a turnover of Rs.1000 crore within a period of two years will have to exit. In this situation investors of exclusively listed companies who are unable to exit will be provided an opportunity to exit through Dissemination Board on the NSE and BSE. While this responsibility of providing exit to investors of exclusively listed companies is primarily of the concerned Stock Exchange

through trading operations, however in view of nil trading this could not be achieved.

The trading at almost all smaller Stock Exchanges have declined and has come to nil in all except one Stock Exchange. Currently, out of the 17 regional recognized Stock Exchanges, trading occurs only at the Calcutta Stock Exchange. These Stock Exchanges can be termed as defunct Stock Exchanges for lack of sustainable operations and the shareholders of companies listed on these Stock Exchanges do not have exit option as these companies do not have listing on Stock Exchanges having nationwide trading terminal. The continued existence of defunct Stock Exchanges requires the SEBI to carry out various regulatory, supervisory and administrative activities which are unproductive and is a regulatory burden. Consequently, and also taking into account the comments of the Ministry of Finance, an exit policy for Stock Exchanges was formulated and brought into effect *vide* the SEBI Circular *vide* December 29, 2008. The new Circular dated May 30, 2012 reviewed the earlier circular of 2008. The Exit Circular issued by the SEBI on May 30, 2012 was issued after deliberation of the matter in the Secondary Markets Advisory Committee (hereinafter referred to as “SMAC”) and SEBI Board. One of the

members of SMAC is the FISE i.e. Federation of Indian Stock Exchanges which has many Stock Exchanges including Respondent No. 3 (VSEL), as its members. FISE had also given its detailed comments on said policy, as a member of the SMAC. Therefore, even the policy relating to the Exit Circular had been finalized after consultation with concerned market participants, though SEBI is not statutorily mandated to undertake prior consultation. The Exit Circular issued by SEBI on May 30, 2012 deals with following aspects viz., voluntary surrender of recognition, compulsory de-recognition, Dissemination Board for companies exclusively listed on the de-recognized Stock Exchanges, Trading Members of de-recognized Stock Exchanges and treatment of assets of de-recognized Stock Exchanges. The annual trading turnover requirement for Stock Exchanges as imposed by the Exit Circular, is by virtue of the powers of de-recognition of Stock Exchanges, given to SEBI in terms of Section 5 of the SCRA. Section 5 of the SCRA reads:-

> *"If the Central Government is of opinion that the recognition granted to a Stock Exchange under the provisions of this Act should, in the interest of the trade or in the public interest, be withdrawn, the Central Government may serve on the governing body of the*

Stock Exchange a written notice that the Central Government is considering the withdrawal of the recognition for the reasons stated in the notice and after giving an opportunity to the governing body to be heard in the matter, the Central Government may withdraw, by notification in the Official Gazette, the recognition granted to the Stock Exchange."

The amount of trading turnover required i.e.1000 crore, is in itself a very small figure when compared to the total trading turnover in the country on an annual basis. If a Stock Exchange is not able to satisfy even this minimum amount, it may be inferred that neither the investors nor the Trading Members of VSEL, are interested in using the platform of such an exchange to deal in securities. The continued existence of such exchanges would be detrimental to the health and safety of the securities market. The trading volumes (equity and equity F&O) on all the Stock Exchanges during the last three years, is as follows:

Trading Turnover details (Amount in Rs. Crore)

Name of the Stock Exchange	2009-10	2010-11	2011-12
BSE	13,78,809	11,05,027	6,67,498
NSE	41,38,023	35,77,410	28,10,892
CSE	1,612	2,597	5,991

UPSE	25	0.12	NIL
VSEL	NIL	NIL	NIL

(The smaller 16 Stock Exchanges do not have any trading/ turnover)

From the above it can be seen that the condition of Rs.1000 crore turnover prescribed is minuscule compared to the trading volumes on the other exchanges. Moreover, a time period of two years has been given to achieve the prescribed turnover of Rs 1000 crores. In fact, the petitioners had stated in para 10 of the petition that "in or around the year 1996-97, the turnover of VSEL was in the range of approximately Rs.10 to 15 crore per day." If this submission is accepted, it may be presumed that the VSEL would, in value terms, be able to achieve an large amounts of trading volume as on date (once the VSEL commences operations) and thereby could easily achieve the requisite trading turnover requirement of Rs.1000 crore. Also, the VSEL has many companies listed on itself and since there are no trading operations, investors do not have an opportunity or a platform to deal in the said shares.

The details of companies listed on the VSEL is as under:

Total no. of companies listed at VSE - 456

Exclusively listed at VSE – 59

Companies not listed at BSE or NSE (excluding exclusively listed companies) – 252

Therefore, the VSE, which is a Stock Exchange, is duty bound to provide trading operations in the scripts listed on itself, an exit mechanism to investors. The VSE is not providing the same since 2003-04 and is not serving the purpose for which it has been granted recognition.

The impugned circular specifies that if the Stock Exchanges are unable to achieve a turnover of Rs.1000 crore within a period of two years they will have to exit. In such a situation investors of exclusively listed companies who are unable to exit will be provided an opportunity to exit through Dissemination Board on Stock Exchanges having nationwide trading. In view of the above the contention of the petitioners that he condition of imposing an annual trading turn over of Rs.1000 crore is unreasonable restriction does not deserve any consideration and deserves to be rejected.

It is further submitted that the Stock Exchanges, in view of the provisions of the SCRA, do not have right to state that the regulator cannot impose any terms and conditions

regarding the functioning and administration of the Stock Exchange. It is further submitted that when the share holders invested in the VSE, there was no trading activity being carried out at the VSE and the Stock Exchange was more in the nature of a defunct Stock Exchange. The major sources of income for the VSEL, as provided in its Annual Reports, may be seen as under:

Major Revenue income of the VSE for last 4 Years.

Particulars	**2008-09**	**2009-10**	**2010-11**	**2011-12**
DP operations	18,325,670	19,990,851	19,926,000	16,309,848
Interest income	9,504,888	21,521,099	21,884,983	24,444,205
Dividend from subsidiary	4,000,000	2,000,000	4,000,000	2,000,000
License fee & additional charges outside terminal	1,521,764	899,783	2,41,19,630	2,611,509
Infrastructure charges (from subsidiary as it shares infrastructure and Man power expenses)	2,286,900	2,515,590	2,767,152	2,898,924

As can be seen from the table above, the income of the VSEL is not from its core function for which it has been granted recognition. The loss of investment for shareholders, if any, is not caused on account of the regulatory structure reviewed by the SEBI, but on account of the investors and brokers not preferring to transact on the VSE. The regulator's functions are done in pursuance of the statutory mandate to protect

investors, regulate and develop the securities market. Hence, the condition imposed by the SEBI is reasonable, just and in the interest of investors.

The averment by the petitioners that the SEBI has absolute control over the Governing Board and therefore they would not take any interest in promoting the growth of the Stock Exchange is absolutely incorrect, misleading, without basis and irrational. Firstly, the Directors on the Governing Board of the Stock Exchanges are not under the absolute control of the SEBI. shareholders Directors are not appointed by the SEBI but are subject to election in the AGM of the Stock Exchange and the approval of the SEBI is based on various criteria including fit and proper person criteria. Also, public interest Directors, whose names are forwarded by the exchange are accorded no objection by the SEBI to the nomination, considering their functions and the need to ensure that such directors must be those who do not have any conflict with its role. Stock Exchanges cannot be viewed only as profit making enterprises. It must balance its objectives of profit making while ensuring that its regulatory functions and investors objectives are served. It is in this context that the SEBI is required to oversee the appointment of Directors so

that management of the Stock Exchanges is undertaken by persons of high caliber, commitment and integrity. Secondly, statistics of attendance of public interest Directors in the meetings of the Governing Boards of various RSEs is an indicator as regards the interest that Public Interest Directors have displayed. Some statistics on this aspect is as follows:

ATTENDANCE OF PUBLIC INTEREST DIRECTORS OF VADODARA Stock Exchange LTD TILL DATE

	Shri Nilknath Jani		**Dr.Samir Joshi**		**Shri Yogendra Shukla**	
Year	**No. of Meetings held**	**No. of Meetings Attended**	**No. of Meetings held**	**No. of Meetings Attended**	**No. of Meetings held**	**No. of Meetings Attended**
2007-08	2	01*	2	01*	1	01**
2008-09	9	9	9	9	9	8
2009-10	7	7	7	7	7	4
2010-11	9	9	9	8	9	7
2011-12	8	7	8	4	8	4
2012-13	-	-	03***	3	-	-

Note: * Appointed on 26th December 2007.

** Appointed on 13th February 2008.

***In the financial year 2012-13, till present date 03 Board Meetings are held.

Shri Nilkanth Jani gave his resignation on 23.02.2012 so there is no question to attend any meeting of FY 2012-13.

Shri Yogendra Shukla gave his resignation on 25.02.2012 so there is no question to attend any meeting of FY 2012-13.

The Depositories Act, 1996 prescribes a net worth requirement of Rs.100 crore for depositories. Further, in the

year 2008, the RBI-SEBI Standing Technical Committee while laying down the procedures for Exchange Traded currency futures prescribed net worth requirement of at least 100 crore rupees as an eligibility criteria for setting up of currency future segment in a recognized Stock Exchange. Further, in the year 2009, the SEBI Board decided that a new exchange shall have net worth of at least Rs.100 crore. Taking it forward the SEBI Board in its meeting held on 2nd April 2012 decided to prescribe the net worth requirement of Rs.100 crore which will be applicable to the Stock Exchanges and Clearing Corporations, by way of impugned regulations. However, looking at the situation of existing Stock Exchanges they were allowed three years time to achieve the same.

The Bimal Jalan Committee also observed that MII (including Stock Exchanges) should be a well-capitalized entity so that the net worth of the MII is available a last resort to meet exigencies and ensure that it is able to remain as a going concern. In view of the above, the impugned regulations prescribed Rs.100 crore net worth criteria, which is very reasonable considering the fact that the functional exchanges already had a higher net worth as follows:

- NSE - Rs.3,316 crore
- BSE - Rs.1463.2 crore
- MCX-SX - Rs.240.39 crore
- CSE - Rs.100 crore
- USEIL – Rs.109 crore

Sections 4A and 4B were inserted in the SCRA to give effect to the Government policy to corporatize and demutualise Stock Exchanges by which ownership, management and trading rights would be segregated from each other. In terms of Section 4B Schemes for Corporatisation and Demutualisation of a Stock Exchange is to be submitted by the concerned exchange for approval by the SEBI. Section 4B provides the SEBI the discretion to approve a scheme and in terms of Section 4B (6), a scheme having such approval would not be restricted in its ambit by any other law in force. In fact, under Section 4B (6), the SEBI may, by order, restrict the voting rights of shareholders who are stock brokers, right of shareholders to appoint representatives on the governing boards and restrict the maximum number of representative of stock brokers to be appointed on the governing board. Approval given by the SEBI of such a scheme reinforces the fact that the SEBI has wide ranging statutory powers to regulate Stock Exchanges in a manner that is in the best

interests of the investors and the securities market.

The Schemes approved by the SEBI under Section 4B do not denude the SEBI of the power to regulate Stock Exchanges through other measures including by way of subordinate legislation or issuance of regulatory directions. The power to regulate the governing board of Stock Exchanges does not solely flow from Section 4B. Such an interpretation would nullify all other provisions of the SCRA as well as the SEBI Act. Also, stating that a scheme once framed under Section 4B would be sacrosanct unto eternity, without leaving any scope for the SEBI as a regulator to review the regulatory structure, would defeat the purpose of regulatory powers conferred on the SEBI by the SCRA and the SEBI Act. Therefore, the contention that the SEBI is denuded of any power to make incursion on the provisions of Sections 3(2) and 4B, is an incorrect understanding of the provisions and framework of the SCRA and is accordingly denied. In fact, proviso to sub-section (1) of Section 4B provides that exchanges which were already corporatized and demutualised do not have to submit a scheme for approval by the SEBI. If the petitioner's argument was to be taken to its logical conclusion, it would mean that the SEBI was powerless to further regulate those exchanges as

regards its ownership and governance structure.

If the SEBI's power to modify schemes for individual Stock Exchanges under Section 4B is recognized, the logical extension of this, considering the SEBI's broad regulatory powers under the Act, would be that the SEBI also has powers with regard to ownership and governance of all Stock Exchanges in general. This power has been exercised by way of framing of regulations. Those aspects of ownership and governance that needed to be clarified by way of circulars, was done so and accordingly the impugned the SEBI Circular dated 13th December 2012 was issued.

Both the impugned SECC Regulations as well as impugned Exit Circular dated 30th May 2012 were issued by the SEBI after due consultation with all stakeholders including the recognized Stock Exchanges, even though there is no statutory mandate for SEBI to make consultations before framing regulations or issuing circulars. In fact, the VSE also had submitted its views on the Bimal Jalan Committee Report and the SMAC Committee decisions (which were the eventual basis on the which SECC Regulations and Exit Circular were framed). Therefore to state that the policy was framed without due

consultation is not factually correct.

Section 5 provides the power to withdraw recognition of Stock Exchanges. This power given to the Central Government is exercised by the SEBI in terms of the notification delegating the power to it. Therefore in terms of Section 5, if the SEBI is in the opinion that the recognition grated to a Stock Exchange under the provisions of the SCRA should, in the interest of trade or public interest, be withdrawn, it may do so after following due procedure under the Act. The reasons for forming such opinion are not objectively outlined in the Act. Therefore the reason on the basis of which such opinion may be formed is left to the discretion of SEBI and may be outlined by way of regulations, circular or any other regulatory direction.

For the purposes of grant of recognition and continuous recognition, the SEBI is empowered to issue conditions and the direct that the rules of Stock Exchange the amendment, if any, and if Stock Exchange fails to amend the rules then the SEBI itself can amend the Rules.

It is open to the SEBI to issue directions as per the provisions of Section 12 (A) to a Stock Exchange in the

interest of investors and the securities market. The SEBI can issue individual directions or conditions to each Stock Exchange or issue the same in composite manner to all the Stock Exchanges by way of circular or instructions. The provision of Section 31 empowers the SEBI to make regulations.

The Securities Contract (Regulation) Act, 1956 being a special enactment will prevail over other Acts including the Companies Act, especially in respect of regulation of Stock Exchanges. The Statement of Objects and Reasons appended to the Bill which was later enacted as SCRA begins with the following sentence:

> "*The object of this Bill is to provide for the regulation of Stock Exchanges and of transactions in securities dealt with in on them. with a view to preventing undesirable speculation in them.*

Also, Section 616D of the erstwhile Companies Act, 1956 reads: "The provisions of this Act, shall apply to any other company governed by any special Act for the time being in force, except in so far as the said provisions are inconsistent with the provisions of such special Act;" A *pari materia*

provision in the new Companies Act, 2013 may be seen in Section 1(4)(e). Therefore, in the case of Stock Exchanges which are companies regulated under the SCRA, the provisions of the Companies Act cannot apply if they are inconsistent with the Act or regulations made thereunder. In the context of Arbitration Act, 1996, the Bombay High Court had noted in the case of *The Stock Exchange, Mumbai v. Vinay Bubna & Others (AIR 1999 Bom 266)* that bye-laws made by the Stock Exchange in pursuance of the mandate under the Securities Contracts (Regulation) Act, 1956 are statutory in nature and, therefore, would prevail over the provisions of the Arbitration Act, 1996. Using the same rationale, subordinate legislation under the SCRA would also necessarily prevail over the provisions of the Companies Act, 2013 since the SCRA is a special statute dealing with Stock Exchanges, though they may be companies. The transition of Stock Exchanges from 'Association of Persons' to companies have, in fact, been promoted by the SEBI under the provisions of the SCRA. Therefore, once they have been corporatized and demutualised in terms of the SCRA, the petitioners cannot argue that the provisions of the SCRA and the SEBI's regulatory purview will no longer prevail. The petitioners' argument amounts to stating that under the provisions of the SCRA, the

SEBI has divested its own powers in favour of the Ministry of Corporate Affairs (MCA) and the Registrar of the Companies (RoC).

Further, certain provisions of the SCRA have been given explicit overriding effect over the Companies Act or any other law for the time being in force. Such provisions include :

(a) power to make rules including the rules restricting voting rights of members, providing restriction on the right of a member to appoint proxy, providing regulation of voting rights so that each member may be entitled to have only one vote irrespective of his share in the paid up equity capital in the Stock Exchange (Section 8 read with Section 7A);

(b) power to restrict the representation of the stock broker on the governing board {Section 4B(6)};

(c) power to restrict the right of shareholders to appoint the representatives on the governing board, {Section 4B(6)};

(d) the manner in which at least 51% of equity share capital of a recognised Stock Exchange is held by the public other than the shareholder having trading rights Section 4B (8)}; and power of SEBI to make rules relating *inter alia* to the governing body of the

Stock Exchange, its constitution and powers of management, duties of office bearers of the Stock Exchange, etc (Section 8 read with Section 3).

The provisions of the SCRA and the provisions of the SEBI Act are relied on for the purposes of passing the impugned regulations and circular. Substantive power to restrict voting rights of shareholders may be traced to Section 4B (6) of the SCRA which provides that voting rights of Stock Broker Shareholders of Stock Exchanges can be restricted. In the present case, the SEBI has imposed such restriction by way of the impugned SECC Regulation. Hence, existence of substantive power regarding imposition of such restrictions is beyond any doubt. This respondent also relies on the provisions of Section 4B, Section 7A of the SCRA for the purposes of demonstrating that this respondent has the power to issue the impugned regulation and circular. Section 7A envisages imposition of such a restriction on the voting rights of the Stock Broker Shareholders. Section 7A exists even prior to introduction of Section 4B. Therefore, the SEBI has got sufficient statutory powers under the SCR Act to impose such a restriction notwithstanding anything contained in the Companies Act, 1956.

The orders of the SEBI (*in terms of Section 4B (1)*) approving the scheme of corporatisation and demutualisation (hereinafter referred to as C&D Scheme) of respective Stock Exchanges, contain a condition to the effect that the SEBI may change the terms of the Scheme in the interest of investors or in the public interest. In particular, para 8.0 of the C&D Scheme of VSE reads as follows:

> "*SEBI reserves rights to amend, alter or modify the Scheme in the interest of the trade and in the public interest and in furtherance of the objectives of the corporatisation and demutualisation of the Stock Exchange.*"

The SCRA gives overriding effect to C & D Scheme once it is approved by the SEBI. Such an approval may be conditional (as mentioned above) or unconditional. Accordingly, Corporatisation & Demutualisation Schemes have overriding effect subject to any condition imposed by the SEBI. The impugned regulations must be seen as directions of the Board modifying the provisions of the Scheme, especially since the impugned regulations, *inter alia*, deal with the manner of demutualisation.

The C & D Scheme of the respective Stock Exchanges, once approved by the SEBI, was required to be incorporated in the Articles of Association/Rules of the respective Stock Exchanges. The SEBI has power under the SCRA to amend the Articles of Association/Rules of Stock Exchanges without any distinction as to whether such Articles of Association/Rules contains the provisions, as approved in the C & D Scheme or other provisions not so approved.

The SEBI is the statutory regulator of the securities market cast with the function of protecting the interests of the securities market, promotion of the development of and regulation of the securities market. Need for granting deference to the views of the expert body has been judicially recognised both globally and within India. In the case of MCX-SX v. SEBI & Ors., the Hon'ble High Court of Bombay (judgment dated March 14, 2012) noted that the SEBI is an expert statutory body and that the High Court would not be justified in substituting the view of an expert adjudicator observed:

> "*While assessing the challenge...the Court must bear in mind that the interference of the Court under Article 226 of the Constitution is confined to certain well settled, if restricted parameters. The view of the expert should not*

be disturbed unless it is perverse or not based on evidence or is based on a misreading of evidence...The High Court under Article 226 of the Constitution would not be justified in substituting the view of an expert adjudicator for another view merely because it commends itself to the Court."

The order of the Securities Appellate Tribunal in the Ketan Parekh matter (SAT order dated 14th July 2006) has also explained lucidly the central relevance of Stock Exchanges in the securities market, *inter alia,* noting that "a Stock Exchange is an association of member brokers, whether incorporated or not, for the purpose of facilitating and regulating the trading in securities" and that Stock Exchanges are platforms for fair price discovery of a scrip based on the market forces of demand and supply.

Net worth requirement is meant for determining the financial health of the company/organization. It is required to ensure that only serious and sound players who can provide the required infrastructure for capital market can enter the market. The impact on the net worth could be very high in extreme scenarios. With depleted net worth Stock Exchange may not be in a position to update and advance its technologies and infrastructure for providing efficient

platform/transaction facility. This may affect to the companies listed on such Stock Exchanges and investors at large. Stock Exchanges provide transaction facility to investors and, thus, discover the price of securities traded on them. Prices provide the signal for efficient allocation of financial resources across corporations. In this sense, the role of the Stock Exchanges in efficient allocation of resource in the economy is of great significance. Recognition to Stock Exchanges is provided for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities. Traditionally, under the open outcry system, a Stock Exchange was understood to be a place where buyers and sellers met in order to buy/sell securities. Over a time, technology has replaced the open outcry system and automated trade engines execute trades based on a price time priority or any other algorithm. To trade through a Stock Exchange, the investor has to become a client of a registered Trading Member of a particular Stock Exchange. Stock Exchanges have been entrusted with various regulatory responsibilities for ensuring market integrity and for protecting the interest of investors. Stock Exchanges, therefore, cannot be seen only as providers of electronic platforms for executing trades. Investor Protection, Better Transparency, Market Integrity, Market Efficiency, Quality of Supervision and

Competitiveness of Financial Markets are very important for building confidence in any financial market. Confidence in financial markets is the main driver encouraging cross-border retail and institutional investment flows. Therefore, a Stock Exchange, apart from providing electronic platforms for executing trades, performs a number of other functions such as issuer regulation (listing, monitoring listing compliances, dissemination of information) member regulation (registration of members, inspection and enforcement action), trading regulation (setting and enforcing trading rules, market surveillance) and investor protection (dispute resolution, grievance redressal, investor protection fund). Securities and Exchange Board of India product design Stock Exchanges also undertake support functions such as training and education, technology solutions, data/information services and index services. Halt in trading may prove detrimental to the interest of investors, companies listed on Stock Exchange, foreign investment and economy of country. As a safety measure to counter any disaster like hacking of trading system, terrorist activity, natural calamity and for ensuring incessant trading in the securities listed on Stock Exchange, Stock Exchanges are also required to maintain a disaster recovery system. Setting up of such disaster recovery system and its maintenance

involves huge cost which calls for huge net worth.

Huge expenditure made by other Stock Exchanges on the technology in the last three years:

Name of the Stock Exchange	**Expenditure (Rs. In crore) during last three financial years**			**Total**
	2010-11	**2011-12**	**2012-13**	
NSE	191.37	185.13	258.13	**634.62**
BSE	59.41	63.54	69.52	**192.47**
MCX-SX	18.84	34.21	123.48	**176.53**

The impugned SECC Regulations aims at complete demutualisation in Stock Exchanges by ensuring that Trading Members or their associates/agents have no role in the management of the Stock Exchanges. This is a step further in making the governing board of the Stock Exchanges without any conflict and in furtherance to the erstwhile Scheme of Corporatisation and Demutualisation.

Corporatisation and Demutualisation of Stock Exchanges was implemented based on the amendment to the SCRA, 1956 through insertion of Sections 4A and 4B. The basis for this amendment actually flows from the Joint Parliamentary Committee Report on Stock Market Scam and Matters Relating

Thereto (2002). In Part I(IX)(4), dealing with the subject of "Demutualisation", the Joint Parliamentary Committee took note of the salient points of change envisaged to be achieved towards demutualisation -

> "***...****Separation of management from ownership For demutualisation, separation of management from ownership is required. Basically, the issue involved is composition of board of directors. To achieve this, either the NSE model may be followed or any of the other patterns followed by international Stock Exchanges which have been corporatized and demutualised could be adopted. Under the NSE pattern there is no broker representation on the Board of the National Stock Exchange of India Limited. NSE has an Executive Committee which has broker representation.*"

The JPC Report stated that there are several models of demutualisation globally. In any case, the JPC recognised the need for Stock Exchanges to be corporatized and demutualised to bring in greater transparency an efficiency of the exchanges and also segregation of trading and ownership.

The recent failure of the National Spot Exchange Limited (NSEL) illustrates the need for adequate capitalization, liquidity and complete separation of management and the interests of Trading Members. The order of the Forward Markets

Commission (FMC) dated 17th December 2013 held that certain promoters and directors of the National Spot Exchange Ltd (NSEL) were not fit and proper persons. The order also reveals certain facts summarised below, which point to the need for better regulation of market infrastructure institutions including Stock Exchanges and clearing corporations.

(i) During the month of July 2013, the NSEL suspended the trading in all contracts (except e-series). The NSEL further suspended the e-series contracts in August 2013. Subsequently, the Forward Markets Commission took steps to ensure settlement of existing contracts. Thereafter, i*nter alia,* the following came to light:

a. The Settlement Guarantee Fund had only 62 crore against 738.55 crore claimed in writing by the NSEL on 1st August 2013.

b. For long term trades the NSEL did not carry out any diligence on the offer letter from the seller or maintain adequate documentation to support the existence of the stock at the designated warehouses.

c. Despite repeated defaults members were allowed to trade and increase their exposure. For example, one of the members had defaulted 198 times during a fifteen month period.

d. Members who were in a default position or who had exhausted their margin limits on trading were granted an exemption from margin requirements. More than 1800 such exemptions were granted between 2009 to 2013.

e. The IBMA, a subsidiary of the NSEL (60.88% stake) was loaned several hundred crore by the NSEL as working capital and provided margin exemption to trade on the NSEL itself, a clear conflict of interest.

(ii) Subsequently, a plan for settlement and meeting payout obligations on installment basis was put into operation, however, the NSEL has defaulted in all six

payouts till date as illustrated below:

Date of Payout	*Amount to be collected from buyers & to be disbursed to the Members as per the settlement plan*	*Amount actually disbursed*	*Short fall*
20.08.2013	*Rs.174.72 crore*	*Rs.92.12 crore*	*Rs.82.60 crore*
27.08.2013	*Rs.174.72 crore*	*Rs.12.60 crore*	*Rs.162.12 crore*
03.09.2013	*Rs.174.72 crore*	*Rs.15.37 crore*	*Rs.159.35 crore*
10.09.2013	*Rs.174.72 crore*	*Rs.13.46 crore*	*Rs.161.26 crore*
17.09.2013	*Rs.174.72 crore*	*Rs. 8.58 crore*	*Rs.166.14 crore*
24.09.2013	*Rs.174.72 crore*	*Rs.11.45 crore*	*Rs.163.27 crore*

Post Dated Cheques deposited with the NSEL were dishonoured on a regular basis. As a result, investors have suffered greatly. It is estimated that around 5500 crore rupees are owed to various investors.

(iii) The gross mismanagement seen in the NSEL matter was further compounded by the lack of adequate net worth leading to the defaults illustrated in para 5. The FMC, in its order dated 17th January 2013 has observed the following "*...establish the fact that the entire*

governance of the company including planning, directing and controlling of its activities was utterly lacking in transparency, integrity, competence, compliance with law, and most importantly an honesty of intent to meet its stated objectives of offering a platform for genuine trading in commodities.

(iv) The NSEL issue as brought out in the above paragraphs clearly illustrates the desperate need for ensuring that the management is independent of control and manipulation by traders and members of exchanges as well as the need for adequate liquidity and capitalisation for meeting exigencies of default so that systemic risks can be avoided.

III. Stance of the respondent no.3 VSEL :

The notice dated 28th November 2012 was issued by the Governing Board of the VSEL in connection with the appointment of four shareholders' directors to give effect to the provisions of the Securities Contracts (Regulation) (Stock Exchange and Clearing Corporations) Regulations, 2012. The notice had to be issued with a view to comply with the SECC

Regulations. The explanatory statement issued by the VSEL pursuant to Section 173(2) of the Companies Act, 1956 reads as under :

"EXPLANATORY STATEMENT PURSUANT TO SECTION 173(2) OF THE COMPANIES ACT, 1956

In respect of business at serial nos.1 to 4

The Governing Board of the Exchange, at its Meeting held on 17th August 2012, framed new composition of the Governing Board of the Exchange in accordance with the provisions of the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012.

Consequently, it was decided that total strength of the Governing Board shall be 12 (Twelve) (excluding Managing Director) comprising of 50% Public Interest Directors and remaining shall be shareholder Directors.

The status of present composition of the Governing Board of the Exchange is as under :

Category	*Available Seats*	*Appointed*	*Vacancy*
Public Interest Director	*6*	*4*	*02**
Shareholder Director	*6*	*2*	*4*
Managing Director	*1*	*-*	*1*

** The Exchange has requested the SEBI for approving two further names of*

Public Interest Directors of the Exchange.

Accordingly, the Exchange has decided to fill up four vacancies in the category of Shareholder Directors in order to comply with SEBI's Guidelines and Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 subject to approval of SEBI. Therefore, the Governing Board of the Exchange recommends the resolutions for approval of the Shareholder.

None of the Members of the Governing Board of the Exchange is interested or concerned in these Resolutions.

Registered Office :

3rd Floor, Fortune Tower
Sayajigunj *By Order of the Board,*
VADODARA – 390 005. *For VADODARA Stock Exchange LTD.*

Sd/-

(M.G.Sheikh)
Officiating Managing Director

Date : 28th November, 2012"

The total strength of the Governing Board shall not exceed twelve (excluding the Managing Director) comprising of atleast 50% public interest directors and the balance shall be the shareholders' directors.

It has been denied that the impugned notice dated 28th November 2012 issued by the Governing Board of the VSEL is illegal or unreasonable in any manner.

IV. Submissions on behalf of the petitioners :

Mr.Mihir Thakore, the learned senior advocate assisted by Ms.Amrita Thakore, the learned advocate appearing for the petitioners, vehemently submitted that the provisions of the circular and the regulations are violative of Articles 14 and 19(1)(g) of the Constitution of India. They do not constitute reasonable restrictions and are, therefore, *ultra vires* the Constitution of India and could be termed as arbitrary, unreasonable and illegal.

Mr.Thakore submitted that although a preliminary objection has been raised on behalf of the respondents as regards the maintainability of this petition, more particularly, the *locus standi* of the petitioners to challenge the impugned circular and the regulations as violative of Articles 14 and 19(1)(g) of the Constitution of India, yet the petition is maintainable as the fundamental rights of the petitioners to trade in securities, as enshrined under Article 19(1)(g) of the Constitution of India, would definitely get affected if the VSEL is derecognized due to non-compliance of the conditions imposed by the SEBI in its circular dated 30th May 2012.

Mr.Thakore submitted that the condition of annual turnover of Rs.1000 crore coupled with the restrictions with regard to the Governing Board, which are imposed by the regulations, in effect, implies that, on the one hand all the Directors are required to be appointed by the SEBI, or subject to approval by the SEBI, i.e. the SEBI has absolute control over the Governing Board of the Stock Exchange, and on the other hand if the very same SEBI controlled Governing Board does not take any initiative or interest in promoting the growth of the Stock Exchange, it would directly affect the interest and business of the other persons like the Trade Members, shareholders, shareholders of the companies listed in such Stock Exchanges. It is submitted that for no fault on the part of such persons, they would lose their means of livelihood.

Mr.Thakore submitted that the SEBI has essentially altered the policy with regard to the Stock Exchanges in India by issuing the circular and the regulations and, therefore, could be said to have exceeded the powers conferred upon it by the Securities Contracts (Regulation) Act, 1956 and the SEBI Act. Mr.Thakore submitted that the impugned circular cannot be termed as law. It is submitted that the circular cannot be

termed as a statutory circular having any force of law even in terms of Article 13 of the Constitution of India. It is further submitted that the invocation of Article 19(6) of the Constitution of India on the basis of the circular is unsustainable in law.

Mr.Thakore, by relying on Section 5 of the SCRA, submitted that a circular cannot be issued as a regulation under Section 31 of the SCRA, or a rule under Section 30 of the Act, 1956.

Mr.Thakore placed reliance on Section 11 of the SEBI Act and submitted that although Section 11 speaks of the powers and functions of the Board, but at the same time speaks of the measures by law, and the circular cannot be termed as law.

Mr.Thakore submitted that Section 8 of the Act, 1956 is confined only to Section 3(2) of the Act and, therefore, the condition of Rs.1000 crore turnover could not have been imposed in exercise of powers under Section 8(1) of the Act.

Mr.Thakore submitted that the conditions could have been prescribed only by the Central Government. Section 4(B)

of the Act, 1956 could not have been exercised by the SEBI in exercise of powers under Section 11 of the SEBI Act.

Mr.Thakore laid much emphasis on the fact that the Scheme was approved by the SEBI and people were invited to invest at a time when there was no condition to achieve turnover of Rs.1000 crore. To achieve the turnover of Rs.1000 crore, adequate platform needs to be created and such a platform has to be created by the Board.

Mr.Thakore, in such circumstances referred to above, prays that there being merit in this petition, the same deserves to be allowed.

V. Submissions on behalf of the respondent no.2 SEBI :

Mr.S.N.Shelat, the learned senior advocate assisted by Ms.Dharmistha Raval, the learned advocate appearing for the SEBI, has raised a preliminary objection as regards the *locus standi* of the petitioners to maintain this petition under Article 226 of the Constitution of India, on the ground that the petitioners cannot assert that they have a fundamental right to

trade in securities only from the VSEL. Mr.Shelat submitted that the total number of Trading Members of the VSEL are 289, of which the present petition has been filed only by 52 persons who are holding 405812 shares of the VSEL, which is 7% of the total share capital of the Stock Exchange. Mr.Shelat submitted that assuming for the moment that the challenge to the policy decision of the SEBI, after consultation with various stake holders, is genuine, even then the petition has not been filed by the affected Stock Exchange. In short, the submission of Mr.Shelat is that there is no opposition at the end of the VSEL to the provisions of the new regulations and the exit circular.

Mr.Shelat submitted that the SCRA, being a special statute, will prevail over the Companies Act.

Mr.Shelat has vehemently opposed this petition and submitted that the impugned circular and the regulations are in no manner violative of Articles 14 and 19(1)(g) of the Constitution of India. Mr.Shelat submitted that the powers exercisable by the Central Government under the SCRA are also exercisable by the SEBI by virtue of general delegation made by the Central Government in favour of the SEBI. Earlier, the Central Government had framed the Securities Contracts

(Regulation) Rules, 1957, however, the administration and enforcement of the SCRR lies with the SEBI.

Mr.Shelat submitted that the impugned regulations have been framed by the SEBI in exercise of its powers conferred by Sections 4, 8A and 31 of the SCRA read with Sections 11 and 30 of the SEBI Act. Under Section 11 of the SEBI Act, the SEBI has been entrusted with the task of protection of investors and development of securities market.

It is submitted that the SEBI has wide powers to protect the interest of the investors and for the development of the securities market.

Mr.Shelat submitted that under Section 12A of the SCRA, the SEBI is also empowered to issue directions to Stock Exchanges, listed companies and other persons associated with the securities market, *inter alia*, in the interest of the investors or orderly development of the securities market.

Mr.Shelat submitted that with such objective in mind, the impugned circular and the regulations have been framed by the SEBI, and for such purpose, the SEBI relied on the Bimal

Jalan Committee report as well as the report of the group on Corporatisation and Demutualisation of Stock Exchanges, headed by Justice M.H.Kania, Former Chief Justice of India, dated 30th January 2003.

Mr.Shelat submitted that the circular has a force of law and could be termed as a statutory circular.

Mr.Shelat lastly submitted that the SEBI is the statutory regulator of the securities market with the function of protecting the interest of the securities market, promotion of development of and regulation of the securities market. Being an expert statutory body, this Court may not substitute the views of such an expert adjudicator. Mr.Shelat submitted that the laws relating to economic activities should be viewed with greater latitude than laws touching the civil rights, such as freedom of speech, religion, etc.

In such circumstances referred to above, Mr.Shelat submitted that there being no merit in this petition, the same deserves to be dismissed.

VI. ANALYSIS :

Having heard the learned counsel appearing for the parties and having gone through the materials on record, the only question that falls for our consideration in this petition is, whether the petitioners are entitled to any of the reliefs as prayed for in this petition.

Since a preliminary objection has been raised by the respondents as regards the *locus standi* of the petitioners to maintain this petition under Article 226 of the Constitution of India, we propose to first deal with such preliminary objection.

Locus standi of the petitioners is a *sine qua non* or condition precedent for the exercise of power or jurisdiction by the Court, inasmuch as, the legal capacity of a party to any litigation, where any private or any public action in relation to a remedy sought has to be decided before granting a relief, the issue as to *locus standi* touches the jurisdiction of the Court.

The issue as to who may file a petition is a fundamental right and has given rise to much debate and controversy, and yet its importance cannot be ignored or underestimated because the Court may not entertain such a petition if not

presented by an aggrieved or interested person.

The traditional rule in regard to the *locus standi* was that the judicial redress was available only to a person who had suffered a legal injury by reason of violation of his legal right or legally protected interest by the impugned action of the State or a public authority or any other person who was likely to suffer a legal injury by a reason of threatened violation of his legal right or legally protected interest by any such action.

The right that can be enforced under Article 226 of the Constitution of India ordinarily shall be personal or individual right of the petitioner himself.

In Jashbhai Motibhai v. Roshan Kumar, (1976)1 SCC 671, after referring to several English, American and Indian cases, the Supreme Court observed that various tests have to be applied to decide whether a person can be said to be an 'aggrieved person'. The Court stated :

> *“Whether the applicant is a person whose legal right has been infringed ? Has he suffered a legal wrong or injury, in the sense that his interest, recognised by law, has been prejudicially and directly affected by the act or*

omission of the authority, complained of ? Is he a person who has suffered a legal grievance, a person against whom a decision has been pronounced which has wrongfully deprived him of something or wrongfully refused him something, or wrongfully affected his title to something ? Has he a special and substantial grievance of his own beyond some grievance or inconvenience suffered by him in common with the rest of the public ? Was he entitled to object and be heard by the authority before it took the impugned action? If so, was he prejudicially affected in the exercise of that right by the act of usurpation of jurisdiction on the part of the authority ? Is the statute, in the context of which the scope of the words 'person aggrieved' is being considered, a social welfare measure designed to lay down ethical or professional standards of conduct for the community ? Or is it a statute dealing with private rights of particular individuals ?"

In the aforesaid context, we propose to also rely upon the following observations of the Supreme Court in the case of Ghulam Qadir v. Special Tribunal, (2002)1 SCC 33, which has been subsequently relied upon by another bench of the Supreme Court in the case of M/s.Tashi Delek Gaming Solutions Ltd. and another v. State of Karnataka and others, reported in AIR 2006 SC 661 :

"38. There is no dispute regarding the legal proposition

that the rights under Article 226 of the Constitution of India can be enforced only by an aggrieved person except in the case where the writ prayed is for habeas corpus or quo warranto. Another exception in the general rule is the filing of a writ petition in public interest. The existence of the legal right of the petitioner which is alleged to have been violated is the foundation for invoking the jurisdiction of the High Court under the aforesaid Article. The orthodox rule of interpretation regarding the locus standi of a person to reach the court has undergone a sea-change with the development of constitutional law in our country and the constitutional courts have been adopting a liberal approach in dealing with the cases or dis-lodging the claim of a litigant merely on hyper-technical grounds. If a person approaching the court can satisfy that the impugned action is likely to adversely affect his right which is shown to be having source in some statutory provision, the petition filed by such a person cannot be rejected on the ground of his having not the locus standi. In other words, if the person is found to be not merely a stranger having no right whatsoever to any post or property, he cannot be non-suited on the ground of his not having the locus standi."

Bearing the aforesaid principle in mind, we proceed to consider the *locus standi* of the petitioners.

It appears from the materials on record that the VSEL,

which is a regional Stock Exchange (RSE) was established in 1990 as a company limited by guarantee, in which ownership and trading rights were vested upon its Trading Members. The petitioners herein are Trading Members and shareholders of the VSEL.

It also appears that the SEBI issued a circular in 1999 permitting the RSEs to acquire membership of the NSE and BSE by floating a subsidiary which would be permitted to acquire membership rights in BSE and NSE.

The members of such RSE were required to register themselves as sub-brokers of the subsidiary to enable them to trade through the subsidiary.

It also appears that the VSEL established a subsidiary called 'VSE Stock Services Limited' (VSSL) for acquiring membership of BSE and NSE. The SCRA was amended to provide for corporatisation (whereby the Stock Exchange would be succeeded by another Stock Exchange which would be a company) and demutualisation (whereby the ownership and management would be segregated to some extent from the trading rights) of Stock Exchanges. In this regard, Sections 4A

and 4B were inserted in the SCRA, *inter alia*, containing the provisions whereby a scheme was required to be approved by the SEBI for corporatisation and demutualisation of each Stock Exchange.

In 2005, the VSEL was converted into a company limited by shares and submitted its Corporatisation and Demutualisation Scheme, 2005, providing, *inter alia*, that 51% share holding would be of the public. Therefore, a share holding of the Trading Members like the petitioners was reduced to 49%.

On 30th May 2012, the SEBI issued a circular stipulating a condition upon the Stock Exchanges of achieving a turnover of Rs.1000 crore on a continuous basis on their own platform, failing which the SEBI would proceed to derecognise such Stock Exchanges. The SEBI, thereafter, issued the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporation) Regulations, 2012, which provides that no Trading Member or clearing member or their associates and agents shall be on the Governing Board of any recognised Stock Exchange. The SEBI also issued a circular stipulating that every recognised Stock Exchange having net worth less than Rs.100

crore as on the date of the commencement of the regulations would be required to submit its plan to the SEBI for achieving the net worth in terms of the regulations within 90 days.

In the aforesaid background, the petitioners who are the Trading Members holding 49% of shares in the company are apprehending that in view of the impugned circular and the regulations their right to trade in securities as enshrined under Article 19(1)(g) of the Constitution of India will get infringed as it is not possible to fulfill the conditions imposed by the SEBI, although in public interest.

We are of the view that although a person may not claim a fundamental right to carry on trade in securities at a particular Stock Exchange only, yet the petitioners as the Trading Members, if prohibited in any manner or are unable to trade on account of the restrictions imposed, it would not prevent them from challenging the constitutionality of the circular or the regulations itself on the ground that it offends against the fundamental right guaranteed under Article 19(1)(g) of the Constitution of India by showing that the restrictions goes in excess of the object or because the activities which are not pernicious are included within the sweep of the statute or

because the procedure laid down in the statute is unreasonable or unjust or arbitrary.

We, thus, reject the preliminary objection raised by the respondents and proceed to consider the submissions on merits.

Before adverting to the rival submissions canvassed on either sides, we deem it necessary to look into various provisions of the SCRA, 1956 and the SEBI Act, 1992 :

Securities Contracts (Regulation) Act, 1956

Section 2 - Definitions

In this Act, unless the context otherwise requires,-

(a) 'Contract' means a contract for or relating to the purchase or sale of securities;

1 ['(aa) "corporatisation" means the succession of a recognised Stock Exchange, being a body of individuals or a society registered under the Societies Registration Act, 1860 (21 of 1860), by another Stock Exchange, being a company incorporated for the purpose of assisting, regulating or controlling the business of buying, selling or

dealing in securities carried on by such individuals or society;

(ab) "demutualisation" means the segregation of ownership and management from the trading rights of the members of a recognised Stock Exchange in accordance with a scheme approved by the Securities and Exchange Board of India;]

2 [3 [(ac)] "derivative" includes--

(A) a security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security;

(B) a contact which derives its value from the prices, or index of prices, of underlying securities]]

(b) 'Government security' means a security created and issued, whether before or after the commencement of this Act, by the Central Government or a State Government for the purpose of raising a public loan and having one of the forms specified in clause (2) of section 2 of the Public Debt Act, 1944 (13 of 1944);

(c) 'member' means a member of a recognised Stock Exchange;

(d) 'option in securities' means a contract for the purchase or sale of a right to buy or sell, or a right to buy and sell, securities in future, and includes a teji, a mandi, a teji mandi, a galli, a put, a call or a put and call in securities;

(e) 'prescribed' means prescribed by rules made under this Act;

(f) 'recognised Stock Exchange' means a Stock Exchange which is for the time being recognised by the Central Government under section 4;

(g) 'rules', with reference to the rules relating in general to the constitution and management of a Stock Exchange, includes, in the case of a Stock Exchange which is an incorporated association, its memorandum and articles of association;

4(ga) "scheme" means a scheme for corporatisation or demutualisation of a recognised Stock Exchange which may provide for-

(i) the issue of shares for a lawful consideration and provision of trading rights in lieu of membership cards of members of a recognised Stock Exchange;

(ii) the restrictions on voting rights;

(iii) the transfer of property, business, assets,

rights, liabilities, recognitions, contracts of the recognised Stock Exchange, legal proceedings by, or against, the recognised Stock Exchange, whether in the name of the recognised Stock Exchange or any trustee or otherwise and any permission given to, or by, the recognised Stock Exchange;

(iv) the transfer of employees of a recognised Stock Exchange to another recognised Stock Exchange;

(v) any other matter required for the purpose of, or in connection with, the corporatisation or demutualisation, as the case may be, of the recognised Stock Exchange;';]

5 [6 [(gb)] "Securities Appellate Tribunal" means a Securities Appellate Tribunal established under sub-section (1) of section 15K of the Securities and Exchange Board of India Act, 1992 (15 of 1992)]

(h) 'securities' include-

(i) shares, scrips stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

7 [(ia) derivative;

(ib) units or any other instrument issued by any

collective investment scheme to the investors in such schemes]

10[(ic) security receipt as defined in clause (zg) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;]

11[(id) units or any other such instrument issued to the investors under any mutual fund scheme;]

12[(ie) any certificate or instrument (by whatever name called), issued to an investor by any issuer being a special purpose distinct entity which possesses any debt or receivable, including mortgage debt, assigned to such entity, and acknowledging beneficial interest of such investor in such debt or receiveable including mortgage debt, as the case may be;]

(ii) Government securities; and

(iii) rights or interests in securities;

8 [(i) "spot delivery contract" means a contract which provides for,-

(a) actual delivery of securities and the payment of a price therefore either on the same day as the date of the contract or on the next day, the actual

period taken for the despatch of the securities or the remittance of money therefore through the post being excluded from the computation of the period aforesaid if the parties to the contract do not reside in the same town or locality;

(b) transfer of the securities by the depository from the account of a beneficial owner to the account of another beneficial owner when such securities are dealt with by a depository;]

9 [(j) "Stock Exchange " means--

(a) any body of individuals, whether incorporated or not, constituted before corporatisation and demutualisation under sections 4A and 4B, or

(b) a body corporate incorporated under the Companies Act, 1956 whether under a scheme of corporatisation and demutualisation or otherwise,

for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities;'.]

Section 3 - Application for recognition of Stock Exchanges

(1) Any Stock Exchange, which is desirous of being recognised for the purposes of this Act, may make an application in the prescribed manner to the Central Government.

(2) Every application under sub-section (1) shall contain such particulars as may be prescribed, and shall be accompanied by a copy of the bye-laws of the Stock Exchange for the regulation and control of contracts and also a copy of the rules relating in general to the constitution of the Stock Exchange, and in particular, to

(a) the governing body of such Stock Exchange, its constitution and powers of management and the manner in which the business is to be transacted;

(b) the powers and duties of the office bearers of the Stock Exchange;

(c) the admission into the Stock Exchange of various classes of members, the qualifications for memberships, and the exclusion, suspension, expulsion and re-admission of members there from or therein to;

(d) the procedure for the registration of partnerships as members of the Stock Exchange in cases where the rules provide for such membership; and the nomination and appointment of authorised representatives and clerks.

Section 4 - Grant of recognition to Stock Exchanges

(1) If the Central Government is satisfied, after making such inquiry as may be necessary in this behalf and after

obtaining such to further information, if any, as it may require,

(a) that the rules and bye-laws of a Stock Exchange applying for registration are in conformity with such conditions as may be prescribed with a view to ensure fair dealing and to protect investors;

(b) that the Stock Exchange is willing to comply with any other conditions (including conditions as to the number of members) which the Central Government, after consultation with the governing body of the Stock Exchange and having regard to the area served by the Stock Exchange and its standing and the nature of the securities dealt with by its, may impose for the purpose of carrying out the objects of this Act; and

(c) that it would be in the interest of the trade and also in the public interest to grant recognition to the Stock Exchange;

it may grant recognition to the Stock Exchange subject to the conditions imposed upon it as aforesaid and in such form as may be prescribed.

(2) The conditions which the Central Government may prescribe under clause (a) of sub-section (1) for the grant of recognition to the Stock Exchanges may include, among other matters, conditions relating to,

(i) the qualifications for membership of Stock Exchanges;

(ii) the manner in which contracts shall be entered into and enforced as between members;

(iii) the representation of the Central Government on each of the Stock Exchanges by such number of persons not exceeding three as the Central Government may nominate in this behalf; and

(iv) the maintenance of accounts of members and their audit by Chartered accountants wherever such audit is required by the Central Government.

(3) Every grant of recognition to a Stock Exchange under this section shall be published in the Gazette of India and also in the Official Gazette of the State in which the principal office of the Stock Exchange is situate, and such recognition shall have effect as from the date of its publication in the Gazette of India.

(4) No application for the grant of recognition shall be refused except after giving an opportunity to the Stock Exchange concerned to be heard in the matter; and the reasons for such refusal shall be communicated to the Stock Exchange in writing.

(5) No rules of a recognised Stock Exchange relating to any of the matters specified in sub-section (2) of section

3 shall be amended except with the approval of the Central Government.

Section 4A - Corporatisation and demutualisation of Stock Exchanges

1[4A. Corporatisation and demutualisation of Stock Exchanges.-

On and from the appointed date, all recognised Stock Exchanges (if not corporatised and demutualised before the appointed date) shall be corporatised and demutualised in accordance with the provisions contained in Section 4B:

Provided that the Securities and Exchange Board of India may, if it is satisfied that any recognised Stock Exchange was prevented by sufficient cause from being corporatised and demutualised on or after the appointed date, specify another appointed date in respect of that recognised Stock Exchange and such recognised Stock Exchange may continue as such before such appointed date.

Explanation.-- For the purposes of this Section, "appointed date" means the date which the Securities and Exchange Board of India may, by notification in the Official Gazette, appoint and different appointed dates may be appointed for different recognised Stock Exchanges]

Section 4B - Procedure for corporatisation and demutualisation

1[Section 4B - Procedure for corporatisation and demutualisation

(1) All recognised Stock Exchanges referred to in Section 4A shall, within such time as may be specified by the Securities and Exchange Board of India, submit a scheme for corporatisation and demutualisation for its approval:

Provided that the Securities and Exchange Board of India, may, by notification in the Official Gazette, specify name of the recognised Stock Exchange, which had already been corporatised and demutualised, and such Stock Exchange shall not be required to submit the scheme under this Section.

(2) On receipt of the scheme referred to in sub-Section (1), the Securities and Exchange Board of India may, after making such enquiry as may be necessary in this behalf and obtaining such further information, if any, as it may require and if it is satisfied that it would be in the interest of the trade and also in the public interest, approve the scheme with or without modification.

(3) No scheme under sub-Section (2) shall be approved by the Securities and Exchange Board of India if the issue of shares for a lawful consideration or provision of trading rights in lieu of membership card of the members of a recognised Stock Exchange or payment of dividends to members have been proposed out of any reserves or

assets of that Stock Exchange.

(4) Where the scheme is approved under sub-Section (2), the scheme so approved shall be published immediately by -

(a) the Securities and Exchange Board of India in the Official Gazette;

(b) the recognised Stock Exchange in such two daily newspapers circulating in India, as may be specified by the Securities and Exchange Board of India,

and upon such publication, notwithstanding anything to the contrary contained in this Act or any other law for the time being in force or any agreement, award, judgment, decree or other instrument for the time being in force, the scheme shall have effect and be binding on all persons and authorities including all members, creditors, depositors and employees of the recognised Stock Exchange and on all persons having any contract, right, power, obligation or liability with, against, over, to, or in connection with, the recognised Stock Exchange or its members.

(5) Where the Securities and Exchange Board of India is satisfied that it would not be in the interest of the trade and also in the public interest to approve the scheme under sub-Section (2), it may, by an order, reject the scheme and such order of rejection shall be published by

it in the Official Gazette:

Provided that the Securities and Exchange Board of India shall give a reasonable opportunity of being heard to all the persons concerned and the recognised Stock Exchange concerned before passing an order rejecting the scheme.

(6) The Securities and Exchange Board of India may, while approving the scheme under sub-Section (2), by an order in writing, restrict-

(a) the voting rights of the shareholders who are also stock brokers of the recognised Stock Exchange;

(b) the right of shareholders or a stock broker of the recognised Stock Exchange to appoint the representatives on the governing board of the Stock Exchange;

(c) the maximum number of representatives of the stock brokers of the recognised Stock Exchange to be appointed on the governing board of the recognised Stock Exchange, which shall not exceed one-fourth of the total strength of the governing board.

(7) The order made under sub-Section (6) shall be published in the Official Gazette and on the publication thereof, the order shall, notwithstanding anything to the contrary contained in the Companies Act, 1956 (1 of

1956), or any other law for the time being in force, have full effect.

(8) Every recognised Stock Exchange, in respect of which the scheme for corporatisation or demutualisation has been approved under sub-Section (2), shall, either by fresh issue of equity shares to the public or in any other manner as may be specified by the regulations made by the Securities and Exchange Board of India, ensure that at least fifty-one per cent. of its equity share capital is held, within twelve months from the date of publication of the order under sub-Section (7), by the public other than shareholders having trading rights:

Provided that the Securities and Exchange Board of India may, on sufficient cause being shown to it and in the public interest, extend the said period by another twelve months.'.]

Section 5 - Withdrawal of recognition

1[5(1)].Withdrawal of recognition.-

(1) If the Central Government is of opinion that the recognition granted to a Stock Exchange under the provisions of this Act should, in the interest of the trade or in the public interest, be withdrawn, the Central Government may serve on the governing body of the Stock Exchange a written notice that the Central Government is considering the withdrawal of the recognition for the reasons stated in the notice, and after

giving an opportunity to the governing body to be heard in the matter, the Central Government may withdraw, by notification in the Official Gazette, the recognition granted to the Stock Exchange;

Provided that no such withdrawal shall affect the validity of any contract entered into or made before the date of the notification, and the Central Government may, after consultation with the Stock Exchange, make such provision as it deems fit in the notification of withdrawal or in any subsequent notification similarly published for the due performance of any contracts outstanding on that date.

2[(2) Where the recognised Stock Exchange has not been corporatised or demutualised or it fails to submit the scheme referred to in sub-Section (1) of Section 4B within the specified time therefor or the scheme has been rejected by the Securities and Exchange Board of India under sub-Section (5) of Section 4B, the recognition granted to such Stock Exchange under Section 4, shall, notwithstanding anything to the contrary contained in this Act, stand withdrawn and the Central Government shall publish, by notification in the Official Gazette, such withdrawal of recognition:

Provided that no such withdrawal shall affect the validity of any contract entered into or made before the date of the notification, and the Securities and

Exchange Board of India may, after consultation with the Stock Exchange, make such provisions as it deems fit in the order rejecting the scheme published in the Official Gazette under sub-Section (5) of Section 4B." .]

Section 12A - Power to issue directions

1[12A. Power to issue directions

If, after making or causing to be made an inquiry, the Securities and Exchange Board of India is satisfied that it is necessary -

(a) in the interest of investors, or orderly development of securities market; or

(b) to prevent the affairs of any recognised Stock Exchange, or, clearing corporation, or such other agency or person, providing trading or clearing or settlement facility in respect of securities, being conducted in a manner detrimental to the interests of investors or securities market; or

(c) to secure the proper management of any such Stock Exchange or clearing corporation or agency or person, referred to in clause (b),

it may issue such directions, -

(i) to any Stock Exchange or clearing corporation or agency or person referred to in clause (b) or any

person or class of persons associated with the securities market; or

(ii) to any company whose securities are listed or proposed to be listed in a recognised Stock Exchange,

as may be appropriate in the interests of investors in securities and the securities market.".]

1 [29A. power to delegate

The Central Government may, by order published in the Official Gazette, direct that the powers (except the power under section 30) exercisable by it under any provision of this Act shall, in relation to such matters and subject to such conditions, if any, as may be specified in the order, be exercisable also by the Securities and Exchange Board of India or the Reserve Bank of India constituted under section 3 of the Reserve Bank of India Act, 1934.]

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1. Substituted by the Securities Laws (Amendment) Act, 1999 w.e.f. 22.02.2000. Prior to its substitution, section 29A read as under:

"*Power to delegate. - The Central Government may, by order published in the Official Gazette, direct that the powers exercisable by it under any provision of this Act shall, in relation to such matters and subject to such conditions, if any, as may bespecified in the order, be exercisable also by the Securities and Exchange Boardof India.*"

Section 30 - Power to make rules

(1) The Central Government may, by notification in the Official Gazette, make rules for the purpose of carrying into effect the objects of this Act.

(2) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for,-

(a) the manner in which applications may be made, the particulars which they should contain and the levy of a fee in respect of such applications;

(b) the manner in which any inquiry for the purpose of recognizing any Stock Exchange may be made, the conditions which may be imposed for the grant of such recognition, including conditions as to the admission of members if the Stock Exchange concerned is to be the only recognised Stock Exchange in the area; and the form in which such recognition shall be granted;

(c) the particulars which should be contained in the periodical returns and annual reports to be furnished to the Central Government;

(d) the documents which should be maintained and preserved under section 6 and the periods for which they should be preserved;

(e) the manner in which any inquiry by the governing body of a Stock Exchange shall be made under section

6;

(f) the manner in which the bye-laws to be made or amended under this Act shall before being so made or amended be published for criticism;

(g) the manner in which applications may be made by dealers in securities for licenses under section 17, the fee payable in respect thereof and the period of such licences, the condition subject to which licences may be granted, including condition relating to the forms which may be used in making contracts, or documents to be maintained by licensed dealers and the furnishing of periodical information to such authority as may be specified and the revocation of licences for breach of conditions;

1[(h) the requirements which shall be complied with--

(A) by public companies for the purpose of getting their securities listed on any Stock Exchange;

(B) by collective investment scheme for the purpose of getting their units listed on any Stock Exchange]

*2[(ha) *******]*

3["(ha) the grounds on which the securities of a company may be delisted from any recognised Stock

Exchange under sub-Section (1) of Section 21A;

(hb) the form in which an appeal may be filed before the Securities Appellate Tribunal under sub-Section (2) of Section 21A and the fees payable in respect of such appeal;

(hc) the form in which an appeal may be filed before the Securities Appellate Tribunal under Section 22A and the fees payable in respect of such appeal;

(hd) the manner of inquiry under sub-Section (1) of Section 23-I;

(he) the form in which an appeal may be filed before the Securities Appellate Tribunal under Section 23L and the fees payable in respect of such appeal;"]

(i) any other matter which is to be or may be prescribed.

4(3)" Every rule made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or both Houses agree that the rule should not be made, the rule shall

thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule."

Section 31 - Power of Securities and Exchange Board of India to make regulations

1[31.Power of Securities and Exchange Board of India to make regulations.

(1) Without prejudice to the provisions contained in section 30 of the Securities and Exchange Board of India Act, 1992, the Securities and Exchange Board of India, may, by notification in the Official Gazette, make regulations consistent with the provisions of this Act and the rules made thereunder to carry out the purposes of this Act.

2[(2) In particular, and without prejudice to the generality of the foregoing power, such regulations may provide for all or any of the following matters, namely: --

(a) the manner, in which at least fifty-one per cent, of equity share capital of a recognised Stock Exchange is held within twelve months from the date of publication of the order under sub-section (7) of section 4B by the public other than the shareholders having trading rights under sub-section (8) of that section;

(b) the eligibility criteria and other requirements under section 17A.]

(3) Every regulation made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the regulation or both Houses agree that the regulation should not be made, the regulation shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that regulation.".

Securities and Exchange Board of India Act, 1992

11. (1) Subject to the provisions of this Act, it shall be the duty of the Board to protect the interests of investors in securities and to promote the development of, and to regulate the securities market, by such measures as it thinks fit.

(2) Without prejudice to the generality of the foregoing provisions, the measures referred to therein may provide for -

(a) regulating the business in Stock Exchanges and any other securities markets;

[(4) Without prejudice to the provisions contained in sub-sections (1), (2), (2A) and (3) and section 11B, the Board may, by an order, for reasons to be recorded in writing, in the interests of investors or securities market, take any of the following measures, either pending investigation or inquiry or on completion of such investigation or inquiry, namely:-

(a) suspend the trading of any security in a recognized Stock Exchange;

(b) restrain persons from accessing the securities market and prohibit any person associated with securities market to buy, sell or deal in securities;

(c) suspend any office-bearer of any Stock Exchange or self-regulatory organization from holding such position;

(d) impound and retain the proceeds or securities in respect of any transaction which is under investigation;

(e) attach, after passing of an order on an application made for approval by the Judicial Magistrate of the first class having jurisdiction, for a period not exceeding one month, one or more bank account or accounts of any intermediary or any person associated with the securities

market in any manner involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder:

> *Provided that only the bank account or accounts or any transaction entered therein, so far as it relates to the proceeds actually involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder shall be allowed to be attached;*

(f) direct any intermediary or any person associated with the securities market in any manner not to dispose of or alienate an asset forming part of any transaction which is under investigation:

> *Provided that the Board may, without prejudice to the provisions contained in sub-section (2) or sub-section (2A), take any of the measures specified in clause (d) or clause (e) or clause (f), in respect of any listed public company or a public company (not being intermediaries referred to in section 12) which intends to get its securities listed on any recognized Stock Exchange where the Board has reasonable grounds to believe that such company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market:*

> *Provided further that the Board shall, either before*

or after passing such orders, give an opportunity of hearing to such intermediaries or persons concerned.]

[Board to regulate or prohibit issue of prospectus, offer document or advertisement soliciting money for issue of securities.

Power to issue directions.

11B. Save as otherwise provided in section 11, if after making or causing to be made an enquiry, the Board is satisfied that it is necessary,-

(i) in the interest of investors, or orderly development of securities market; or

(ii) to prevent the affairs of any intermediary or other persons referred to in section 12 being conducted in a manner detrimental to the interest of investors or securities market; or

(iii) to secure the proper management of any such intermediary or person, it may issue such directions,-

(a) to any person or class of persons referred to in section 12, or associated with the securities market; or

(b) to any company in respect of matters specified

in section 11A, as may be appropriate in the interests of investors in securities and the securities market]

29.(1) The Central Government may, by notification, make rules for carrying out the purposes of this Act.

(2) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely:-

(a) the term of office and other conditions of service of the Chairman and the members under sub-section (1) of section 5;

(b) the additional functions that may be performed by the Board under section 11;

(c)[****]

(d) the manner in which the accounts of the Board shall be maintained under section 15;

(da) the manner of inquiry under sub-section (1) of section 15-I;

(db) the salaries and allowances and other terms and conditions of service of the [Presiding Officers, Members] and other officers and employees of the Securities Appellate Tribunal under section 15-O and sub-section (3) of section 15S;

(dc) the procedure for the investigation of misbehaviour or incapacity of the [Presiding Officers, or other Members] of the Securities Appellate Tribunal under sub-section (3) of section 15Q;

(dd) the form in which an appeal may be filed before the Securities Appellate Tribunal under section 15 -T and the fees payable in respect of such appeal;]

(e) the form and the manner in which returns and report to be made to the Central Government under section 18;

(f) any other matter which is to be, or may be, prescribed, or in respect of which provision is to be, or may be, made by rules.

Power to make regulations.

30. (1) The Board may, [***] by notification, make regulations consistent with this Act and the rules made thereunder to carry out the purposes of this Act.

(2) In particular, and without prejudice to the generality of the foregoing power, such regulations may provide for all or any of the following matters, namely:-

(a) the times and places of meetings of the Board

and the procedure to be followed at such meetings under sub-section (1) of section 7 including quorum necessary for the transaction of business;

(b) the terms and other conditions of service of officers and employees of the Board under sub-section (2) of section 9;

(c) the matters relating to issue of capital, transfer of securities and other matters incidental thereto and the manner in which such matters shall be disclosed by the companies under section 11A;

(d) the conditions subject to which certificate of registration is to be issued, the amount of fee to be paid for certificate of registration and the manner of suspension or cancellation of certificate of registration under section 12.]

Rules and regulations to be laid before Parliament.

31. Every rule and every regulation made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or regulation or both Houses agree that the rule or regulation should not be made, the rule or regulation

shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule or regulation.

Application of other laws not barred.

32. The provisions of this Act shall be in addition to, and not in derogation of, the provisions of any other law for the time being in force."

VII. Object of establishment of the SEBI :

To understand the object, it is necessary to know the background of the legislation and the object and scheme of the Act as well.

"The Securities and Exchange Board of India Ordinance, 1992", "to provide for the establishment of a Board to protect the interests of investors in securities and to promote the development of, and to regulate the securities market and matters connected therewith or incidental thereto" was promulgated on January 30, 1992. This Ordinance was converted into an Act viz. "The Securities and Exchange Board of India Act, 1992 by Parliament in April 1992. What prompted the Government to place in position a legislation focussed on

investor protection is evident from the following Objects and Reasons of the Bill. -

> "*The capital market has witnessed tremendous growth in recent times characterised particularly by the increasing participation of the public. Investor's confidence in the capital market can be sustained largely by investor protection. With this end in view Government decided to clothe SEBI immediately with statutory powers required to deal effectively with all matters relating to capital market.*"

Section 3 of the Act provides for establishment of a Board namely the "Securities and Exchange Board of India", for the purposes of the Act. The purposes of the Act according to its preamble are to "provide for the establishment of a Board to protect the interests of investors in securities and to promote the development of, and to regulate, the securities market and for matters connected there with or incidental thereto"

Chapter IV of the Act is on "powers and functions" of the Board. Section 1 1 therein enumerates the functions of the Board. Sub section (1) of section 1 1 provides that subject to the provisions of the Act, it shall be the duty of the Board to protect the interests of investors in securities and to promote the development of, and to regulate the securities market, by

such measures as it thinks fit. Sub section (2), provides without prejudice to the generality of sub section (1) certain specific measures for the purpose. One of the specific measures provided therein is the provision for registering and regulating the working of several types of capital market intermediaries, including Bankers to an Issue.

The Act was further amended in 1995, because: -

> "*On the basis of past experience of the Board a need has been felt to amend the said Acts (i.e. SEBI Act and Securities Contracts (Regulation) Act), in respect of certain categories of intermediaries, persons associated with the securities market and companies on matters relating to issue of capital and transfer of securities*".

Accordingly, several amendments were made to the Act, most of them intended to strengthen the Respondent's role as protector of investors' interest. "In order to enable the Board to function more effectively", the Board was given power to issue directions. It is needless to say that investors by and large are often at the receiving end in the hands of certain unscrupulous market players. There was no focussed attention to protect their interests in the securities market. Their plight was in no way different from the plight of consumers. In view of the comparable position in which the investors and the consumers

are placed, it is felt appropriate to cite the following observations made by the Supreme Court in Lucknow Development Authority Vs. M.K.Gupta ((1994) SCC 243): recognising the need for specific consumer protection legislation enacted by the Parliament and a constructive approach in interpreting the provisions of the law. The Supreme Court observed that:

> " *it appears appropriate to ascertain the purpose of the Act, the objective it seeks to achieve and the nature of social purpose it seeks to promote as it shall facilitate in comprehending the issue involved and assist in construing various provisions of the Act effectively. To begin with the preamble of the Act, which can afford useful assistance to ascertain the legislative intention, it was enacted, ' to provide for the protection of the interest of consumers*'. *Use of the word, protection*' *furnishes key to the minds of makers of the Act. Various definitions and provisions which elaborately attempt to achieve this objective have to be construed in this light without departing from the settled view that a preamble cannot control otherwise plain meaning of a provision. In fact the law meets long felt necessity of protecting the common man from such wrongs for which the remedy under ordinary law for various reasons has become illusory. Various legislations and regulations permitting the State to intervene and protect interest of the consumers have become a haven for unscrupulous ones as the enforcement machinery either does not move or it*

moves ineffectively, inefficiently and for reasons which are not necessary to be stated. The importance of the Act lies in promoting welfare of the society by enabling the consumer to participate directly in the market economy. It attempts to remove the helplessness of a consumer which he faces against powerful business, described as ' a network of rackets' or a society in which, producers have secured power' to 'to the rest' and the might of public bodies which are degenerating into storehouses of inaction where papers do not move from one disk to another as a matter of duty and responsibility but for extraneous consideration leaving the common man helpless, bewildered and shocked. The malady is becoming so rampant, widespread and deep that the society instead of bothering, complaining and fighting against it, is accepting it as part of life".

The aforenoted observations, in our opinion, are applicable with all force to the case at hand.

The Apex Court in the said decision had also Provided guidance for the benefit of the Courts in interpreting such a beneficial legislation: Since the SEBI Act is also a beneficial legislation the approach of the courts in interpreting its provisions should not be different. Following extract from the decision provides the guidance:

"*The provisions of the Act thus have to be construed in*

favour of the consumer to achieve the purpose of enactment as it is a social benefit oriented legislation. The primary duty of the court while construing the provisions of such an Act is to adopt a constructive approach subject to that it should not do violence to the language of the provisions and is not contrary to the attempted objective of the enactment".

Thus, from the above it is clear that the Securities and Exchange Board of India (SEBI) was established in 1988 through a Government Resolution to promote orderly and healthy growth of the securities market and for investors protection. The SEBI has been monitoring the activities of the Stock Exchanges, mutual funds, merchant bankers, etc. to achieve this goals. It is an Act to provide for the establishment of the Board to protect the interests of the investors in securities and to promote the development and to regulate the securities market and for matters connected therewith or incidental thereto.

The Securities Contracts (Regulation) Act, 1956 is an Act to prevent undesirable transactions in securities by regulating the business of dealing therein by providing for certain other matters connected therewith.

At this stage, it may not be out of place to make a mention of the three notifications issued by the Ministry of Finance. They are as under :

"MINISTRY OF FINANCE

(Department of Economic Affairs)

NOTIFICATION

New Delhi, the 30th July, 1992

S.O. 573(E). - In exercise of the powers conferred by section 29A of the Securities Contracts (Regulation) Act, 1956 (42 of 1956), the Central Government hereby directs that the powers exercisable by it under sub-section (5) of section 4, section 7, section 8, section 11, section 12 and section 16 of the said Act shall also be exercisable by the Securities and Exchange Board of India.

[F. No.1(27)SE/92]

KAMAL PANDE, Jt.Secy."

"MINISTRY OF FINANCE

(Department of Economic Affairs)

(ECB and Investment Division)

NOTIFICATIONS

New Delhi, the 13th September, 1994

S.O. 672(E). - In exercise of powers conferred by Section 29A

of the Securities Contracts (Regulation) Act, 1956 (42 of 1956), the Central Government hereby directs that the powers exercisable by it under section 3, sub-sections (1), (2), (3) and (4) of section 4, section 5, sub-section (2) of section 7A, section 13, sub-section (2) of section 18, section 22, and sub-section (2) of section 28 of the Act shall also be exercisable by the Securities and Exchange Board of India.

[F. No.1/57/SE/93]

P.J. NAYAK, Jt.Secy."

"NOTIFICATION

Mumbai, the 30th December 2013

No.LAD-NRO/GN/2013-14/35/7326.- The Securities and Exchange Board of India, having considered the application for renewal of recognition made under Section 3 of the Securities Contracts (Regulation) Act, 1956 by Vadodara Stock Exchange Limited having its registered office at 3rd Floor, Fortune Tower, Sayajigunj, Vadodara 390005 and being satisfied that it would be in the interest of the trade and also in the public interest so to do, hereby grants, in exercise of the powers conferred under Section 4 of the Securities Contracts (Regulation) Act, 1956, renewal of recognition to the said Exchange under Section 4 of the said Act for a period of one year commencing on the 4th day of January, 2014 and ending on 3rd day of January, 2015 in respect of contracts in securities subject to the conditions stated herein below or as prescribed or imposed hereafter :

The exchange can commence trading in securities only after complying with all the regulatory requirements imposed by the Securities and Exchange Board of India including full compliance with Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulation, 2012.

The exchange shall comply with such other conditions as may be prescribed by SEBI from time to time.

RAJEEV KUMAR AGARWAL, Whole Time Membership

[ADVT.III/4/Exty./69-ZB/13]"

Thus, from the above, it is clear that Section 29A of the Act, 1956 provides for delegation of powers exercisable by the Central Government to the SEBI by an order of the Central Government, in relation to such matters and subject to such conditions as may be specified in the order. In terms of the notifications referred to above, the SEBI was invested with the power to grant/withdraw the recognition to a Stock Exchange including the powers exercisable under the provisions of the SCRA referred to in the notifications.

We now propose to look into few decisions of the Supreme Court, wherein the power of the SEBI and the

legislative intent for enacting the SEBI Act has been explained.

In Securities and Exchange Board of India v. Ajay Agarwal, AIR 2010 SC 3466, the Supreme Court considered the question, whether Section 11B of the Securities and Exchange Board of India Act could be invoked by the Chairman of the SEBI in conjunction with Sections 4(3) and 11 for restraining the respondent of that case from associating with any corporate body in accessing the securities market and prohibiting him from buying, selling or dealing in securities. While considering the said question, the Supreme Court made the following observations, which are worth noting :

> *"39. If we look at the legislative intent for enacting the said Act, it transpires that the same was enacted to achieve the twin purposes of promoting orderly and healthy growth of securities market and for protecting the interest of the investors. The requirement of such an enactment was felt in view of substantial growth in the capital market by increasing participation of the investors. In fact such enactment was necessary in order to ensure the confidence of the investors in the capital market by giving them some protection.*
>
> *40. The said Act is pre-eminently a social welfare legislation seeking to protect the interests of common men who are small investors.*

41. It is a well known canon of construction that when Court is called upon to interpret provisions of a social welfare legislation the paramount duty of the Court is to adopt such an interpretation as to further the purposes of law 18 and if possible eschew the one which frustrates it.

42. Keeping this principle in mind if we analyse some of the provisions of the Act it appears that the Board has been established under Section 3 as a body corporate and the powers and functions of the Board have been clearly stated in Chapter IV and under Section 11 of the said Act.

43. A perusal of Section 11, Sub-Section 2(a) of the said Act makes it clear that the primary function of the Board is to regulate the business in Stock Exchanges and any other securities markets and in order to do so it has been entrusted with various powers.

44. Section 11 had to be amended on several occasions to keep pace with the `felt necessities of time'. One such amendment was made in Sub Section (4) of Section 11 of the said Act, which gives the Board the power to restrain persons from accessing the securities market and to prohibit such persons from being associated with securities market to buy and sell or deal in securities. Such an amendment came in 2002.

45. From the statement of objects and reasons of the

Amendment Act of 2002, it appears that the Parliament thought that in view of growing importance of stock market in national economy, SEBI will have to deal with new demands in terms of improving organisational structure and strengthening institutional capacity.

46. Therefore, certain shortcomings which were in the existing structure of law were sought to be amended by strengthening the mechanisms available to SEBI for investigation and enforcement, so that it is better equipped to investigate and enforce against market malpractices. (See Paragraph 3 of the Statement of objects and reasons).

47. Section 11B which empowers the Board to issue certain directions also came up by way of amendment in 1995 by Act 9 of 1995. The Statements of Objects and Reasons of such amendments show one of the objects is to empower the Board to issue regulations without the approval of the Central Government. (See para 3(e) of the Statements of Objects and Reasons). Section 11B of the Act thus empowers the Board to give directions in the interest of the investors and for orderly development of securities market, which, as noted above, is one of the twin purposes to be achieved by the said Act. Therefore, by the 1995 amendment by way of Section 11B Board has been empowered to carry out the purposes of the said Act."

In N.Narayan v. Adjudicating Officer, SEBI, AIR 2003 SC 3191, while considering the unfair trade practices relating to securities market and the market abuse, the Court made the following observations, which are worth noting :

"25. In Sahara India Real Estate Corporation Limited and Others v. Securities and Exchange Board of India and Another (2013)1 SCC 1, this Court has noticed that though the Indian Companies Act, 1956 was modeled on English Companies Act, 1948, no efforts have been made to incorporate universally accepted principles and concepts into our company law. Of late, however, some efforts have been made by carrying out few amendments to the Companies Act, 1956, so also in the SEBI Act, 1992 and Rules and Regulations framed therein to keep pace with the English Companies Act and related legislations. When we interpret the provisions of the SEBI Act and the Regulations relating to a company registered under the Companies Act, the provisions of the Companies Act have also to be borne in mind. For instance, in SEBI Act, there is no provision for keeping proper books of accounts by a registered company.

26. Section 209 of the Companies Act says that every company shall keep at the registered office proper books of accounts. Books of accounts should be so kept as to give true and fair view of the state of the company's affairs and explain transactions. Of course, the auditors of the company must examine whether the company has

maintained proper cost accounting records as required by the rules. Companies whose securities are traded on a public market, it is trite law that the disclosure of information about the company is crucial for the correct and accurate pricing of the company's securities and for the official operation of the market. Section 210 of the Companies Act states that at every annual general meeting of the company, the Board of Directors is required to lay before it a balance-sheet as at the end of and a profit and loss account for the financial year.

27. Clause 41 of Listing Agreement between the SEBI and the concerned companies requires the companies to furnish to Stock Exchange and to publish unaudited financial result on a quarterly basis in the prescribed format. Section 55A of the Companies Act deals with the powers of SEBI which says some of the provisions referred to therein, so far as they relate to issue and transfer of securities and non-payment of dividends in the case of listed companies be administered by SEBI. Further, it is also indicated that how the books of accounts have to be kept by the company, so also with regard to audit of account etc. finds a place in the Companies Act, so also the qualification and disqualification of the Managing Directors.

28. We notice in this case that the Directors of the company had clearly violated provisions of Section 12A of SEBI Act read with Regulations 3 and 4 of 2003 Regulations. Companies whose securities are traded on a

public market, disclosure of information about the company is crucial for the accurate pricing of the companies' securities and also for the efficient operation of the market.

Corporate Governance and Directors

29. SEBI Act read with Regulations of the Companies Act would indicate that the obligations of the Directors in listed companies are particularly onerous especially when the Board of Directors makes itself accountable for the performance of the company to share holders and also for the production of its accounts and financial statements especially when the company is a listed company.

30. The Directors of the company or the person in charge directly or indirectly use or employ, in connection with the issue, purchase or sale of any securities listed in Stock Exchange, any manipulative or deceptive device or contrivance in contravention of SEBI Act or the Regulations made thereunder have necessarily to be dealt with in accordance with the provisions of the Act and the Regulations which is absolutely necessary for the investor's protection and to avoid market abuse."

In Bhavesh D.Parish and others v. Union of India and another, 2005(5) SCC 471, the issue before the Supreme Court was the validity of Section 9 of the Reserve Bank of India Act, on the ground that the said provision was violative of Articles

14 and 19(1)(g) of the Constitution of India. While considering the validity, the Supreme Court made the following observations in paras 22, 23 and 24, which are worth noting :

"22. The RBI has not acted hastily. Before amending Section 45-S of the Act in 1997, it had the benefit of having with it the reports of number of committees, all of whom had recommended that the unincorporated business firms/individuals be brought under certain discipline and, if possible, non-banking financial business was not to be permitted to be carried on by the unincorporated bodies. It will be useful in this regard to refer to the report of the study group on non-banking financial intermediaries appointed by the Banking Commission in 1971. The study group after making a detailed study of the then existing non-banking financial intermediaries stated in respect of unincorporated bodies in para 8.25 of its report as under:

> *"8.25 We, therefore, suggest that the Reserve Banks control may be extended to finance corporations and necessary enabling legislation be passed to that effect. We recognise that the administrative task of watching and regulating the operations of a large number of small firms will be difficult. We, therefore, suggest that if the law permits, only companies may be allowed to do the banking business in the sense of accepting deposits from the public for the purpose of lending or investment. IN that case, the Banking Regulation Act would govern the operations of the Bangalore type finance corporations. If,*

however, the law does not permit it, any scheme of regulation may have as one of its objections the reduction in the number of finance corporations besides, of course, the safeguarding of depositors interest."

23. It was further submitted that the amendments were introduced after taking into account the recommendations of successive committees, appointed by the Bank and Government of India, which had studied the functioning of these bodies. The question of restricting such financial activity by unincorporated bodies, is a question of economic policy as it involves regulation of economic activities by different constituents. In such matters of economic policy, this Honble Court does not interfere with the decision of the expert bodies which have examined the matter. The following observations of this Honble Court made in R.K. Garg Vs,. Union of India, 1982 (1) SCR 947 at 969 are appropriate:

"Another rule of equal importance is that laws relating to economic activities should be viewed with greater latitude than laws touching civil rights such as freedom of speech, religion etc. It has been said by no less a person than Holmes,J. that the legislature should be allowed some play in the joints, because it has to deal with complex problems which do not admit of solution through any doctrinaire or straight jacket formula and this is particularly true in case of legislation dealing with economic matters, where, having regard to the nature of the problems required to be dealt with, greater play in the joints has to be allowed to the legislature. The court

should feel more inclined to give judicial deference to legislature judgment in the field of economic regulation than in other areas where fundamental human rights are involved. Nowhere has this admonition been more felicitously expressed than in Morey V. Dond (354 US 457) where Frankfurther J. said in his inimitable style:

> *"In the utilities, tax and economic regulation cases, there are good reasons for judicial self-restraint if not judicial deference to legislative judgment. The legislature after all has the affirmative responsibility. The courts have only the power to destroy, not to reconstruct. When these are added to the complexity of economic regulation, the uncertainty, the liability to error, the bewildering conflict of the experts, and the number of times the judges have been overruled by events self limitation can be seen to be the path to judicial wisdom and institutional prestige and stability."*

> *The court must always remember that legislation is directed to practical problems, that the economic mechanism is highly sensitive and complex, that many problems are singular and contingent, that laws are not abstract propositions and do not relate to obstract units and are not to be measured by abstract symmetry that exact wisdom and nice adaptation of remedy are not always possible and that judgement is largely a prophecy based on meager and uninterrupted experience. Every*

legislation particularly in economic matters is essentially empiric and it is based on experimentation or what one may call trial and error method and therefore it cannot provide for all possible situations or anticipate all possible abuses. There may be crudities and inequities in complicated experimental economic legislation but on that account alone it cannot be struck down as invalid."

At page 988 it is further held:

"That would depend upon diverse fiscal and economic considerations based on practical necessity and administrative expediency and would also involve a certain amount of experimentation on which the court would be last fitted to pronounce. The court would not have the necessary competence and expertise to adjudicate upon such an economic issue. The court cannot possibly assess or evaluate what would be the impact of a particular immunity or exemption and whether it would sere the purpose in view or not."

24. Even if these restrictions incorporated in the Act amount to a total prohibition, such action was necessary in the public interest as the mushroom growth of unincorporated bodies accepting deposits had gone beyond control calling for restriction of the nature imposed by the amended Section 45-S. In the case of

Reserve Bank of India Vs. Peerless General Finance and Investment Co. Ltd. and others (1987) 61 Company Cases 663, this Honble Court took judicial notice of and expressed concern about the mushroom growth of such bodies by referring to the advertisements issued by various such bodies in the press. While upholding the constitutional validity of the Prize Chits and Money Circulation Schemes (Banning) Act, 1978 (Srinivasa Enterprises Vs. Union of India, 1980 (4) SCC 507) this Honble Court pointed out that for saving the poor and unwary public from the unscrupulous racketeers who glamourise and prey upon the gambling instinct to get rich through prizes, banning was necessary. The court observed how can you save moth from the fire except by putting out the fatal fire ? On the same analogy for safeguarding or protecting the public from the loss which was likely to be caused to them by the failure of unincorporated bodies promising high returns, it was necessary to prohibit unincorporated bodies from accepting deposits from the public. Further, as observed by this Court in Srinivas Enterprises case (supra) it is a constitutional truism that restrictions in extreme cases should be pushed to the point of prohibition, if any lesser strategy will not achieve the purpose."

In Madhubhai Amathalal Gandhi v. Union of India, AIR 1961 SC 21, the challenge before the Supreme Court was a notification dated 31st August 1957 recognising the Stock Exchange, Bombay, under Section 4 of the Securities Contracts

(Regulation) Act, 1956. The Supreme Court noted briefly while examining the legality and validity of the notification how a Stock Exchange works and how it is controlled or regulated by the State. The following observations made by the Supreme Court are worth noting :

> *“At the outset it is necessary to notice briefly how a Stock Exchange is worked and how it is controlled or regulated by the State. 'Stock Exchange' means, "any body of individuals, whether incorporated or not, constituted for the purpose of assisting or controlling the business of buying, selling or dealing in securities”. The history of Stock Exchanges in foreign countries as well as in India shows that the development of joint stock enterprise would never have reached its present stage but for the facilities which the Stock Exchanges provided for dealing in securities. They have a very important function to fulfill in the country's economy. Their main function, in the words of an eminent writer, is 'to liquify capital by enabling a person who has invested money in, say, a factory or a railway, to convert it into cash by disposing of his share in the enterprise to someone else'. Without the Stock Exchange, capital would become immobilized. The proper working of a Stock Exchange depends upon not only the moral stature of the members but also on their caliber. It is a trite saying that a jobber or dealer is born and not made. In the words of the same author, a jobber must be a man of good nerve, cool judgment, and ready to deal under any ordinary*

conditions, and he must be a man of financial standing, considerable experience, with an understanding of market psychology. There are three modes of dealing in shares and stores, namely, (1) spot delivery contract, i.e., a contract which provides for the actual delivery of securities on the payment of a price thereof either on the day of the contract or the next day, excluding perhaps the period taken for the despatch of the securities or the remittance of money from one place to another; (2) ready delivery contract, which means a contract for the purchase or sale of securities for the performance of which no time is specified and which is to be performed immediately or within a reasonable time; (3) forward contracts, i.e., contracts whereunder the parties agree for their performance at a future date. If the Stock Exchange is in the hands of unscrupulous members, the second and third categories of contracts to buy or sell shares may degenerate into highly speculative transactions or, what is worse, purely gambling ones. Where the parties do not intend while entering into a contract of sale or purchase of securities that only difference in prices should be paid, the transaction, even though speculative, is valid and not void, for 'there is no law against speculation as there is against gambling'. But, if the parties do not intend that there should be any delivery of the shares but only the difference in prices should be accounted for, the contract, being a wager, is void. More often than not it is difficult for a court to distinguish one from the other, as a wagering transaction may be so cleverly camouflaged as to pass off as a speculative transaction. These mischievous potentialities

inherent in the transactions, if left uncontrolled, would tend to subvert the main object of the institution of Stock Exchange and convert it into a den of gambling which would ultimately upset the industrial economy of the country."

"After the Act came into force, both the Exchanges applied for recognition under the Act. The Government, after considering the relative merits and the relevant circumstances, issued a notification dated August 31, 1957, recognising the Native Share and Stock Brokers' Association under the name 'The Stock Exchange, Bombay' subject to the conditions mentioned therein. One of the conditions imposed was that the members of the Indian Stock Exchange Limited would be entitled to apply for membership of the Stock Exchange, Bombay, provided they were active members of the Indian Stock Exchange Limited for 12 months immediately preceding August 6, 1957, and they were also eligible under R.8(1) of the Securities Contracts (Regulation) Rules, 1957, to be members of a recognised Stock Exchange. The notification further gave some concessions to such active members in the matter of payment of the membership fee. They had to apply for membership before October 15, 1957, or before such period as the Board of the recognised Stock Exchange might think fit to extend. It appears that within the extended time a number of active members of the Indian Stock Exchange Limited as defined by the notification applied for membership and were admitted as members of the recognised Stock

Exchange. Though three years have passed by, no member other than the petitioner has so far thought fit to question the validity of the notification, that is, the validity of the notification has been accepted and the recognised Stock Exchange has become stabilised on that basis. Subsequent to the filing of. the petition on November 30, 1957, the Central Government issued another notification applying S.13 of the Act to Greater Bombay; with the result that thereafter every contract in shares between the members of any unrecognised Stock Exchange in that City would be illegal."

"Re. (1): Article 19(1)(g) of the Constitution states that every citizen shall have the right to carry on any business; but the State in empowered under cl. (6) of the said Article to make any law imposing in the interest of the general public reasonable restrictions on the exercise of the said right. Briefly stated, the argument is that the combined effect of the two notifications is that the petitioner is driven out of his business of Stock Exchange in as much as, it is said, they confer a monopoly on the Stock Exchange, Bombay, and the rules of the said Stock Exchange exclude any outsider from becoming its member without obtaining a nomination and that too only in the place of an existing member. To put it differently, the argument proceeds that under the rules of the Stock Exchange, Bombay, membership is not thrown open to the public. This leads us to the consideration of the relevant provisions of the Stock Exchange Rules, Bye-laws and Regulations, 1957. Under

R.3 the membership of the Exchange shall consist of such number of members as the Exchange in general meeting may from time to time determine. It is common case that the membership of the Exchange is not limited. Under the heading 'Election of New Members', the Rules prescribe the conditions of eligibility for election as a member of the Exchange. These Rules adopt the provisions of R. 8 of the Securities 201 Contracts (Regulation) Rules, 1957. The Rules do not contain any limitation on the eligibility of a person to be elected as a member such as that the person, should be nominated in the manner provided by the Rules or that he should come only in the vacancy caused by another member ceasing to be one in one of the ways mentioned thereunder. The words 'no person' in R.17 are comprehensive enough to take in any outsider seeking for election as a member. Rule 22 provides for an application for admission in the form prescribed in Appendix A to the Rules. This rule also does not impose any such limitation. The admission application form in Appendix A is also general in terms and enables any person of India to apply for membership provided he agrees to abide by the conditions imposed therein. In the form also there is no such limitation. But it is contended that a fair reading of the provisions of Rr. 20 and 21 makes it clear that a candidate for admission is confined only to two categories, viz., (1) a candidate nominated by a member or a legal representative of a deceased member seeking admission to membership in the place of' the deceased; and (2) a person recommended for admission to membership in the place of a member who has forfeited his right to membership.

A careful scrutiny of the Rules does not bear out the contention; nor do they enable us to cut down the wide amplitude of Rr. 17 to 22. Rule 10 says:

> "*When a right of membership is forfeited to or vests in the Exchange under any Rule, Bye-law, or Regulation of the Exchange for the time being in force it shall belong absolutely to the Exchange free of all rights, claims or interest of such member or any person claiming through such member and the Governing Body shall be entitled to deal with or dispose of such right of membership as it may think fit.*"
>
> *Rule 54 is to the following effect:*
>
> " *A member's right of membership shall lapse to and vest in the Exchange immediately be is declared a defaulter.*" *Rule 11 is as follows..*
>
> "*(a) A member of not less than seven years' standing who desires to resign may nominate a person eligible under these Rules for admission to membership of the Exchange as a candidate for admission in his place*
>
> *(b) The legal representatives of a deceased member or his heirs or the persons mentioned in Appendix C*

to these Rules may with the sanction of the Governing Board nominate any person eligible under these Rules for admission to membership of the Exchange as a candidate for admission in the place of the deceased member. In considering such nomination the Governing Board shall be guided so far as practicable by the instructions set out in Appendix C to these Rules."

Appendix B gives the nomination forms Nos.1 and 2 to be filled by a member or a legal representative, as the case may be, under R.11 (a) and (b). Now it would be convenient to read Rr. 20 and 21. They are as follows:

Rule 20: "A candidate for admission except' a candidate applying for a membership vesting in the Exchange must obtain a nomination in the manner provided in these Rules."

Rule 21: "A candidate for admission must be recommended by two members none of whom should be a member of the Governing Board. The recommenders must have such personal knowledge of the candidate and of his past and present circumstances as shall satisfy the Governing Board."

The argument is that under R.20 a candidate for ad.

mission falls under two categories, namely, (1) a candidate who must obtain a nomination in the manner provided in the Rules, i.e., R.11(a) and (b); and (2) a candidate applying for a membership vesting in the Exchange; and, therefore, these two categories exhaust the candidates for admission and that when under r. 21 the same words, 'a candidate for admission', are used they must carry the same meaning as in R.20, that is, they must be confined only to the two categories comprehended by R.20. This argument appears to be plausible and even incontrovertible, if Rr. 20 and 21 are taken out of their setting and construed independently of other rules. But in the setting in which they appear they can bear only one meaning, namely, that R.20 provides for nomination only in the case of a candidate for admission who requires a nomination in the manner provided by the rule and R.21 provides, for all the candidates for admission, that they should be recommended by two members who have personal knowledge of the candidates. To put it in other words, under the Rules candidates for admission fall under three groups, viz., (1) candidates falling under R.11, (a) and (b); (2) candidates applying for membership vesting in the Exchange; and (3) other candidates. All the three categories of candidates must be recommended by two members. But the candidates belonging to the first category shall in addition be nominated in the manner provided by the Rules. We, therefore, hold that the Stock Exchange Rules do not operate as a bar against the petitioner becoming a member of the Stock Exchange subject to the rules governing such application. The

petitioner has the right to do business in shares: in spite of the notifications he can still do business in spot delivery contracts. He can apply to become a member of the Stock Exchange subject to the conditions laid down by the Rules. The Act the validity of which he has not chosen to question, enables the State to give or refuse recognition to any Stock Exchange and it has chosen to give recognition to the Stock Exchange, Bombay, subject to the conditions prescribed. The restrictions, in our view, are not unreasonable, having regard to the importance of the business of a Stock Exchange in the country's national economy and having regard to the magnitude of the mischief sought to be remedied in the interest of the general public. At another place we have already dealt with the necessity for stringent rules governing this type of business For the reasons Mentioned we reject the first contention."

"There is a presumption in favour of the State that there is a reasonable basis for the classification. Except the mere allegations in the affidavit which are not admitted, the petitioner has not placed before us any materials to ascertain that any other members, who were regularly doing business on the floor of the Indian Stock Exchange Limited before August 6, 1956, temporarily suspended their business for one reason or other over which they had no control. No statement from the accounts has been produced to enable us to evaluate the activities of the members before the crucial date so as to enable us to form a view that really active members were excluded by

the fixing of this period. Nor are we in a position to verify whether any of the members excluded were regularly doing business during a part of the year in continuation of their business in the earlier period. We cannot also say that the words "carrying on business regularly" are so vague that the parties did not understand their connotation, for it is admitted that some of the regular members applied for membership of the Stock Exchange, Bombay and most of them were admitted. There is also the fact that though three years have elapsed since the date of the notification no other member of the Indian Stock Exchange Limited thought fit to question the notification on the ground that the period fixed was unreasonable and that really active members were excluded from membership of the Stock Exchange, Bombay. So far as the petitioner is concerned, he was admittedly not an active member, though lie now pretends that he was doing business through other members. There is also no material placed before us to support the said assertion. If the classification, between active members and others who were not, is justifiable-we hold it is-the Government has to draw a line somewhere and to fix a period of activity reasonable in its opinion as a standard to satisfy the test of " active member ". The burden which lies upon the petitioner who impeaches the validity of the classification to show that it violates the guarantee of equal protection has not been discharged. On the material placed before us we cannot say that the period fixed by the Government as the standard for ascertaining the active membership is arbitrary or unreasonable. We must make it clear that

this finding must be confined only to the validity of the impugned notification dated August 31, 1956."

In the case of Securities and Exchange Board of India v. Alka Synthetics Ltd., 1999(1) GLR 275, a Division Bench of this Court has observed as under :

"...While considering the question as to whether the SEBI has the authority of law under the existing statute to impound or forfeit the monies, we may observe in the very beginning that the learned single judge has approached and decided this question on the basis of the principles of law, which have been laid down by the courts in matters relating to fiscal and taxing statutes and the inhibition against the imposition of levy and collection of any tax and the consequential deprivation of property. In our considered opinion, the very approach and the principles on which this question has been decided by the learned single judge were not at all germane because here is a case in which the court is concerned with the provisions of a comprehensive legislation, which was enacted to give effect to the reformed economic policy investing the SEBI with statutory powers to regulate the securities market with the object of ensuring investors' protection, the orderly and healthy growth of the securities market so as to make the SEBI's control over the capital market to be effective and meaningful. The SEBI Act is an Act of remedial nature and, therefore, the present cases could

not be compared with the cases relating to the fiscal or taxing statutes or other penal statutes for the purposes of collection and levy of taxes, etc. As and when new problems arise, they call for new solutions and the whole context in which the SEBI had to take a decision, on the basis of which the impugned orders were passed cannot be said to be without authority of law in face of the provisions contained in section 11 and section 11B of the Act. As the languagd of section 11(1) itself shows and as the matters for which the measures can be taken are provided in sub-section (2) of section 11. It is clearly made out by a plain reading of the language of the section itself that the SEBI has to protect the interests of the investors in securities and has to regulate the securities market by such measures as it thinks fit and such measures may be for any or all of the matters provided in sub-section (2) of section 11 and in due discharge of this duty cast upon the SEBI as a part of its statutory function, it has been invested with the powers to issue directions under section 11B."

Thus, from the aforesaid decisions, it is amply clear that under Section 11 of the SEBI Act, the SEBI has to protect the interest of the investors in securities and to regulate the securities market by such measures as it thinks fit and such measures may be for any or all of the matters provided in sub-section (2) of Section 11, and in due discharge of its duties cast upon the SEBI as part of its statutory function, it has been

invested with the powers to issue directions under Section 11B. The SEBI is invested with the statutory powers to regulate the securities market with the object of ensuring investors' protection, orderly and healthy growth of securities market so as to make the SEBI's control over the capital market to be effective and meaningful. The SEBI has to regulate speculative market, and in case of speculative market, varied situations may arise and looking into the exigencies and requirements, it has been entrusted with the duties and functions to take such measures as it thinks fit. Section 11B of the SEBI Act is an enabling provision enacted to empower the SEBI Board to regulate securities market in order to protect the interest of the investors. Such an enabling provision must be so construed as to subserve the purpose for which it has been enacted. The SEBI is charged with the duty to protect the public and the integrity of the capital market, and as a regulator, it has powers to issue the circular impugned in this petition in public interest including the regulations, and the interference at the end of the court in such type of matters should be minimal unless it is established that the same is in gross violation of any of the provisions of law or the Constitution of India.

It appears from the materials on record that the SEBI

considered various reports of the experts on the issue and the impugned circular and the regulations are based on the findings recorded in the report of the experts.

We shall now look into the Report of the Group on Corporatisation and Demutualisation of Stock Exchanges headed by Justice M.H.Kania, Former Chief Justice of India, dated 30th January 2003 :

> *"**4. Existing structure of the Stock Exchanges in India** 4.1 In terms of the legal structure, the Stock Exchanges which are recognised under the Securities Contracts (Regulation) Act in India, could be segregated into two broad groups – 20 Stock Exchanges which were set up as companies, either limited by guarantees or by shares, and the 3 Stock Exchanges which are functioning as associations of persons (AOP) viz. BSE, ASE and Indore Stock Exchange. The 20 Stock Exchanges which are companies are: the Stock Exchanges of Bangalore, Bhubaneswar, Calcutta, Cochin, Coimbatore, Delhi, Gauhati, Hyderabad, Interconnected SE, Jaipur, Ludhiana, Madras, Magadh, Managalore, NSE, Pune, OTCEI, Saurashtra-Kutch, Uttar Pradesh, and Vadodara. Of these, the Stock Exchanges of Ahmedabad, Bangalore, BSE, Calcutta, Delhi, Hyderabad, Madhya Pradesh, Madras and Gauhati were given permanent recognition by the Central Government at the time of setting up of these Stock*

Exchanges. Apart from NSE, all Stock Exchanges whether established as corporate bodies or Association of Persons (AOPs), are non-profit making organizations.

4.2 It is thus clear that BSE, ASE and Indore Stock Exchange will have to be both corporatised and demutualised, while of the balance 20 Stock Exchanges, 18 Stock Exchanges which are already corporate entities, will only have to be demutualised. Two Stock Exchanges, NSE and OTCEI, are not only corporatised but also demutualised with segregation of ownership and trading rights of members. Further, NSEIL is a for-profit company and the Board of NSEIL comprises of representatives of shareholders, (some of whom have 100% stock broking subsidiaries) and outside non-shareholder directors. But even these two Stock Exchanges may if necessary, have to undergo changes in organizational structure consequential to the recommendations of the Group so that a common structural model is adopted by the all the Stock Exchanges.

4.3 The present status as above along with the details of the assets and liabilities of some major Stock Exchanges in India is enclosed in (Annexure 5A and 5B).”

“5.7 Demutualisation involves the segregation of members' right into distinct segments, viz. ownership rights and trading rights. It changes the relationship between members and the Stock Exchange. Members while retaining their trading rights acquire ownership

rights in the Stock Exchange, which have a market value, and they also acquire the benefits of limited liability. The shareholders in a corporatised Stock Exchange may be a diverse group, as members may decide to retain their shares or to sell them. Demutualisation however, does not insulate them from competition. A Stock Exchange whose management does not effectively work to maintain its position in the market may soon become a take-over target."

"9. The Stock Exchanges, which had demutualised have followed different models. However, a common feature has been that members surrender their mutual membership rights and in lieu thereof, they are issued shares in the demutualised company. The number of shares issued has some relationship to the value of the assets of the Stock Exchange. In several cases, a public issue of shares was also made."

"5. A basic character of the Stock Exchanges in India, saving NSE, irrespective of their legal constitution, is that they are meant to be voluntary, not for-profit mutual entities. It is on this ground that the Stock Exchanges (except NSE) have claimed tax exemptions, though in dispute in some cases. Demutualisation fundamentally alters this position of the Stock Exchanges, as these would no longer retain their voluntary, not for-profit mutual character, but become for-profit corporate bodies. The most critical part of demutualisation exercise is to work out a blue print to manage this transition in a

smooth manner."

"8. In view of the arguments in the foregoing paragraphs, the Group recommends that -

> *a) as corporatisation and demutualisation of a Stock Exchange is essentially a conversion from a not-for profit entity to a for-profit company, and would result in a distribution of assets, the Income Tax Act should be amended if necessary, so that the past profits of an Stock Exchange which were not taxed when it had the character of a not for profit entity should not be taxed when its character changes. In other words, the accumulated reserves of the Stock Exchange as on the day of corporatisation should not be taxed. However, there would be no objection to taxation of these reserves, in the hands of the shareholders when these are distributed to shareholders as dividend at the net applicable tax rate; equally all future profits of the Stock Exchange after it becomes a for profit company may be taxed;"*

<u>"Segregation of trading rights and ownership</u>

9.19 For the purpose of segregation of ownership and trading rights, the Group examined the present systems of membership prevailing in the Stock Exchanges in the country. It was noted that except for NSE, which offers trading rights against deposits, all other Stock Exchanges

have the concept of membership cards for their members. In some Stock Exchanges e.g. BSE, the trading right is exercised through the ownership of a trading card, which subject to BSE's approval can be transferred for a consideration. Cards can be sold by members and also by the Stock Exchange when new members are introduced."

"Governance of the Stock Exchanges

9.22 The Group noted that in the past, in almost all the Stock Exchanges, the broker members of the governing boards have been critical in the governance of the Stock Exchanges. The reconstitution of the governing boards of the Stock Exchanges by SEBI, which reduced the broker representation on these boards to 50%, had helped in making the boards more independent and minimised the influence of brokers. However, in most Stock Exchanges on account of the brokers retaining posts of the officer bearers of the Stock Exchanges till recently viz. president, vice-president and treasurer, they continued to play a dominant role in the management of the Stock Exchange. The fall-out of this practice has been that most Stock Exchanges have failed to develop good corporate governance practices and strong management teams. This has not only been a perception but also a reality in most Stock Exchanges. Conflicts of interest have bedeviled the operations of the Stock Exchanges in the past to the detriment of the securities market. If the Stock Exchanges are to function in a modern competitive environment these deficiencies would have to be

removed and they would have to adhere to the high standards of corporate governance. Indeed this is one of the objectives to be achieved through this entire exercise of demutualisation of the Stock Exchanges."

"24. Divergent views have been expressed on the issue of broker representation on the governing boards of Stock Exchanges. The case for broker representation has been made by almost all Stock Exchanges and brokers' association. Their argument is that the brokers are major stakeholders in a Stock Exchange and they are affected by the manner in which an Stock Exchange functions. They also have the experience and knowledge of the market and therefore should have some representation on the governing boards of the Stock Exchanges. Besides, the demutualised corporatised structure envisages that brokers could continue to be shareholders and as such be eligible to be elected on the boards as directors. The investors' association have made the case for not giving any representation to the brokers. The argument against broker representation is one of conflict of interest and the possibility of interference and exercising influence in the functioning of the Stock Exchange. The investors' association have felt that in a sense the presence of brokers on the governing boards affects the independence of the executives of the Stock Exchange who may be answerable to the very persons whose actions they are expected to control."

"26. The issues of conflict of interest which may have

arisen in the Stock Exchanges in the past could be further addressed separately, by building up strong management teams and putting in place appropriate systems and procedures which would ensure that brokers are not able to interfere in the day to day functioning of the Stock Exchanges. The Group therefore recommends that –

> *a. the three stakeholders viz. shareholders, brokers and investing public through the regulatory body should be equally represented on the governing board of the demutualised Stock Exchange;*
>
> *b. to f. xxx xxx xxxx*
>
> *g. the maximum number of directors on the board will be governed by the relevant provisions of the Companies Act. 1956;"*

"32. The Stock Exchanges and brokers' association have represented to the Group that with the advent of NSE and the trading by NSE and BSE on a national scale, most of the Stock Exchanges have nil or negligible turnover. Further the regional Stock Exchanges have invested considerable sums in computerization and on-line trading systems which have now become virtually redundant. Many Stock Exchanges have therefore, formed subsidiary companies which have become members of NSE and BSE and members of the Stock Exchange function as sub-brokers of these companies. This has enabled brokers of

these Stock Exchanges to trade on NSE and BSE without acquiring the membership of these Stock Exchanges. Under these circumstances, the prevailing view in most Stock Exchanges and among the brokers seems to veer towards closure of the Stock Exchanges. In this context, the overwhelming concern is one of finding a suitable exit route that will enable the members to recoup the investments made by them in those Stock Exchanges."

"9.40 In order to explore the possibilities of utilisation of the existing IT infrastructure put in place by all these Stock Exchanges the Group examined the Euronext initiative in Europe, which has led to the merger of the Stock Exchanges of Paris, Brussels and Amsterdam. The Euronext Stock Exchange now allows for the creation of a common order book for any share listed on any of the three Stock Exchanges. The trading is done on a common trading platform. The Euronext trades are settled through Clear Net, which acts as a common clearing house acting as counter party and the Euro Clear which acts as a depository. The key to the success of the Euronext appears to be the unification of the back offices, the order book, harmonization of the trading platforms of the three Stock Exchanges and a single clearing house have contributed to the success of Euronext despite the Stock Exchanges being under three different regulatory regimes."

"9.44 In sum, the Group is of the view that –

a. *uniform model for corporatisation and demutualisation would have to be adopted by all the Stock Exchanges. This model should not be made applicable selectively only for a few Stock Exchanges;*

b. *if the recommendations are adopted and suitable legislative changes carried out to implement the recommendations, the Stock Exchanges will be required to submit a scheme of demutualisation to SEBI by an appointed date, and non-compliance in this regard would result in lapse of recognition granted to an existing Stock Exchange, whether permanent or temporary;*

c. *merger of Stock Exchanges, before or after demutualisation is a commercial decision and the choice should be left to the concerned Stock Exchanges and it is not within the purview of the Group to recommend a specific course of action. However, the Group strongly feels that corporatisation and demutualisation will facilitate the process of consolidation of Stock Exchanges; and*

d. *while the Group does not wish to recommend measures which may provide an exit route to the members of the Stock Exchanges, any Stock Exchange which fails to comply with the requirement of corporatisation and*

demutualisation by the appointed date and is accordingly derecognised, will have to distribute its assets in accordance with the provisions of the respective articles/ rules of the Stock Exchange and the relevant tax laws shall become applicable."

"Legal changes required

9.45 The Group felt that some of the provisions in the various relevant statutes would have to be amended to implement the recommendations. Without these amendments it would be difficult to enforce the recommendations. The Group noted that the Stock Exchanges and the representatives of brokers have also suggested similar changes. The Group also noted that in several countries such as Australia and Singapore, a separate Act was passed to give effect to demutualisation. Among the statutes which require changes here are the Securities Contract (Regulations) Act, 1956, the Income Tax Act, 1961 and the Indian Stamps Act, 1899. The Group therefore recommends that-

the relevant provisions of the Securities Contract (Regulations) Act, 1956, the Income Tax Act, 1961 and the Indian Stamps Act, 1899 be suitably amended to facilitate corporatisation and demutualisation of the Stock Exchanges and to grant fiscal exemptions to encourage this process."

*"**4. Recommendations***

The recommendations of the Group are as follows:i. a) the Stock Exchanges which are set up as association of persons and those which are set up as companies limited by guarantee be converted into companies limited by shares;

b) a common model for corporatisation and demutualisation be adopted for all Stock Exchanges; and

c) the clause (j) of section 2 of SCRA be amended to mean that the Stock Exchanges could be companies incorporated under the companies act. The present provisions under clause (j) of section of 2 of SCRA defines Stock Exchanges to "mean any body of individuals, whether incorporated or not, constituted for the purpose of assisting regulating or controlling the business of buying, selling or dealing in securities". This clause would need to be amended to provide that a Stock Exchange should be a company incorporated under the Companies Act."

"iv.a) the three stakeholders viz. shareholders, brokers and investing public through the regulatory body should be equally represented on the governing board of the demutualised exchange;"

"viii. There should be a ceiling of 5% of the voting rights which can be exercised by a single entity or groups of related entities, irrespective of the size of ownership of

the shares."

"xi. On the issue of alternative use of the existing infrastructure facility of the Stock Exchanges, the Group was of the view that that some of the Stock Exchanges could explore the possibility of merger on the lines of Euronext. The Group does not recommend any specific route as being mandatory as the choice should be dictated on commercial considerations. The Group however feels that it would be in national interest that the infrastructure available with the Stock Exchanges be put to best economic use. In case the Stock Exchanges adopt the Euronext model, SEBI will have to work out the eligibility criteria for the brokers, model rules and bye-laws for such an Stock Exchange, the risk containment measures, and the listing guidelines."

VIII. Legality and validity of the impugned circular :

The above takes us to consider the contention canvassed on behalf of the petitioners as regards the legality and validity of the circular in question. It has been strenuously contended before us by Mr.Thakore, the learned senior advocate appearing for the petitioners that the impugned circular has no force in law and cannot be termed as a statutory circular. In short, the sum and substance of the submission canvassed on

behalf of the petitioners is that, if the SEBI wanted to introduce the exit policy for derecognized/non-operational Stock Exchanges by imposing a condition of a turnover of Rs.1000 crore on continuous basis, the same could have been done only by enacting a law within the meaning of Article 13 of the Constitution of India, otherwise a circular will have no force of law.

We are not impressed by such submission of Mr.Thakore. First, in the circular issued by the SEBI, it has been stated that the same has been issued in exercise of powers conferred under Sections 11(1) and 11(2)(j) of the SEBI Act, 1992 read with Section 5 of the SCRA Act, 1956, to protect the interests of investors in securities and to promote the development of and to regulate the securities market. Thus, it is clear that the circular has been issued with a particular object and in exercise of the statutory power conferred on the SEBI as a statutory authority. Whether a circular issued by a statutory authority would be binding or not, or whether the same has a statutory force or not, would depend upon the nature of the statute. For the said purpose, the intention of the Legislature must be considered.

The Supreme Court, in the case of Sudhir Shantilal Mehta v. C.B.I., AIR 2009 SCW 5709, had considered an identical issue with the only distinguishing feature that in that case the circular was issued by the Reserve Bank of India exercising control over the banking companies. The Supreme Court made the following observations, which are worth noting :

“...Having regard to the fact that the Reserve Bank of India exercises control over the Banking Companies, we are of the opinion that the said Circular letter was binding on the Banking Companies. The officials of UCO Bank were, therefore, bound by the said circular letter.

The Madhya Pradesh High Court in The State of Madhya Pradesh v. Ramcharan [AIR 1977 MP 68] held:

"*6. Although the Constitution does not contain any generic definition of law, it defines "law" for purposes of Article 13 to include "any Ordinance, order, bye-law, rule, regulation, notification, custom or usage having in the territory of India the force of law". Article 366(10) of the Constitution also defines the expression "existing law" to mean "any law, Ordinance, Order, bye-law, rule or regulation passed or made before the commencement of this Constitution by any legislature authority or person*

having power to make such law, Ordinance, order, bye- law, rule or regulation". Another definition which is relevant here is the definition of the expression "Indian law" in the General Clauses Act, 1897. Section 3(29) of this Act defines "Indian Law" to mean "any Act, Ordinance, regulation, rule, order or bye-law, which before the commencement of the Constitution had the force of law in any Province of India or part thereof and hereafter has the force of law in any Part A State or Part C State or part thereof, but does not include any Act of Parliament of the United Kingdom or any Order in Council, rule or other instrument made under such Act". These definitions go to confirm that under our legal order "law" does not include only legislative enactments but it also includes rules, orders, notifications etc. made or issued by the Government or any subordinate authority in the exercise of delegated legislative power.

... 7. The question relating to a post-constitution order or notification in the context whether it amounts to law was considered by the Supreme Court in Jayantilal Amratlal v F. N. Rana, AIR 1964 SC 648. ...The Court further observed as follows:

> *"This is not to say that every order issued by an executive authority has the force of law. If the order is purely administrative, or is not issued in exercise of any statutory authority it*

> *may not have the force of law. But where a general order is issued even by an executive authority which confers power exercisable under a statute, and which thereby in substance modifies or adds to the statute, such conferment of powers must be regarded as having the force of law.*" ..."

The issue as regards the statutory force of a circular has been considered by the Supreme Court in connection with the binding nature of the Reserve Bank of India guidelines in the following two decisions :

(i) B.O.I. Finance Ltd. v. The Custodian and others, AIR 1997 SC 1952

(ii) Central Bank of India v. Ravindra and others, AIR 2001 SC 3095.

While examining the Securities Contracts (Regulation) Act and the Banking Regulation Act in B.O.I. Finance Ltd.(*supra*), the Supreme Court specifically dealt with the provisions of Section 36(1)(a) which empowers the RBI to auction or prohibit the banking companies generally or any banking company in particular against entering into any particular transaction and generally to give advice to any banking companies, and held that a circular issued by the RBI which stated that the banks

were advised to follow the Guidelines given thereunder, the word 'advised' cannot be read in isolation and the said document was meant to be binding on the banking companies.

In the case of Central Bank of India (*supra*), the Supreme Court observed that the RBI is a prime banking institution of the country entrusted with a supervisory role over banking and conferred with the authority of issuing binding directions, having statutory force, in the interest of public in general and preventing banking affairs from deterioration and prejudice as also to secure the proper management of any banking company generally. It was further observed as below :

> *"...RBI has been issuing directions/circulars from time to time which, inter alia, deal with rate of interest which can be charged and the periods at the end of which rests can be struck down, interest calculated thereon and charged and capitalised. It should continue to issue such directives. Its circulars shall bind those who fall within the net of such directives. For such transaction which are not squarely governed by such circulars, the RBI directives may be treated as standards for the purpose of deciding whether the interest charged is excessive, usurious or opposed to public policy."*

In the aforesaid connection, our attention has been drawn by Mr.Shelat, the learned senior advocate appearing for the SEBI to one more decision of the Supreme Court in the case of J.K.Vasavada and others v. Chandrakanta Chimanlal Bhavsar and another, AIR 1975 SC 2089.

In the said case, the appellants before the Supreme Court as well as the respondents were originally servants of the State of Bombay and were allotted to the State of Gujarat on its formation on 1st May 1960. The respondents alleged that they had passed all the prescribed departmental examination as required by the rules of the State of Bombay and challenged the validity of certain orders of the Government of Gujarat. One of those was an order which provided that persons already promoted would have to pass the examination of G.D.C. & A. within a period of three years and if they failed to do so, then their increment would be stopped and if they had reached the maximum of the scale, their pay would be reduced to the next lower stage, until they passed the examination. In short, the main grievance of the respondents before the High Court of Gujarat was the laying down of the qualification of G.D.C. & A. for the purposes of earning increments as well as promotion. The question before the Supreme Court was as to what were

the conditions of service applicable immediately before the appointed day to the parties in that case. The conditions of service applicable included not merely the rules made under the proviso to Article 309 of the Constitution of India but also included the liability to be subjected to any other rule that might be made under that proviso. In respect of all Government servants who were allotted to the reorganized State of Bombay, Section 115(7) of the States Reorganisation Act, 1956 was made applicable. It was under the proviso to that section that the circular was issued by the Government of India. Under that circular, it was opened to the reorganized State of Bombay to make any rules for promotion of its servants which were not applicable to them before the formation of the reorganized State of Bombay. While considering such issue, the Supreme Court made the following observations :

> *“We may in this connection refer to s. 87 of the Bombay Reorganisation Act, 1960 which reads:*
>
> > "*87. Territorial extent of laws.-The provisions of Part II shall not be deemed to have effected any change in the territories to which any law in force immediately before the appointed day extends or supplies, and territorial reference in any such law to*

the State of Bombay shall until otherwise provided by a competent legislature or other competent authority, be construed as meaning the territories within that State immediately before the appointed day."

Law is defined in that Act in s. 2(d) as follows:

"*law*" *includes any enactment, ordinance, regulation, order, bye-law, rule, scheme, notification or other instrument having, immediately before the appointed day, the force of law in the whole or in any part of the State of Bombay;*"

The memorandum of Central Government dated 11th May, 1957 was an approval in terms of the proviso to sub-section (7) of section 115 of the States Reorganisation Act. It is, therefore, an order or other instrument having the force of the law for the purposes of the definition of 'law'. That circular had certainly the force of law in the whole of the State of Bombay and as s. 87 provides that law would continue to be in force within the territories of the State of Bombay immediately before the appointed day which, included the territories of the State of Maharashtra as well as the State of Gujarat the reference to the State Governments in the circular would include reference to the Governments of the State or Maharashtra and the State of Gujarat. It should, therefore, be held that even in terms of the circular of the Central Government dated 11th May, 1957 the

Gujarat Government was competent to make the rules which they had made in 1962. The argument on behalf of the petitioners therefore that no approval could have been, given in terms of section 87 of the Bombay Reorganisation Act by a circular issued even in 1957 before that Act was passed has no force."

A Division Bench of the Bombay High Court, in the case of Stock Exchange, Mumbai v. Vinay Bubna and others, AIR 1999 Bombay 266, had also the occasion to consider such issue, more particularly, the interpretation of the word 'enactment'. We quote the following observations made in paras 37, 38 and 39 :

"37. It is well settled that subordinate or delegated legislation takes different forms. Subordinate legislation is divided into two main classes, namely, (a) statutory rules and (b) bye-laws or regulations made by (i) authorities concerned with local Government and (ii) persons, societies or Corporation. This is clearly enunciated in the judgment of the Apex Court in Dr.Indramani Pyarelal Gupta and others v. W.R. Natu and others, to which a reference has been made in paras 26 and 27 above. Again, in the case of the Trustees of the Port of Madras v. M/s. Aminchand Pyarelal and others, the Apex Court observed that a bye-law is an ordinance affecting the public, or some portion of the public, imposed by some authority clothed with statutory

powers, ordering something to be done or not to be done, and accompanied by some sanction or penalty for its non-observance.

38. We may at this stage refer to the dictionary meaning of the word "enactment". In "The Oxford Companion to Law" by David M.Walker, 1980 edition at page 401, the word "enactment" has been defined to include a statutory instrument, bye-law or other statement of law made by a person or body with legislative powers by the appropriate means." The exact definition may be reproduced. "Enactment" A general term for a statute or Act of Parliament, statutory instrument, bye-law or other statement of law made by a person or body with legislative powers by the appropriate means." In the dictionary of Modern Legal Usage, second edition, by Bryan A. Garner, at page 313, the word "enactment" has been defined to have more than one sense namely (i) the action or process of making (a legislative bill) into law; enactment of the bills; or (ii) a statute - a recent enactment - As far as the sense (iii) is concerned, it means "statute or Act of Parliament; statutory instrument, bye-law or other statement of law made of a person or body with legislative powers.

39. In P.Ramanatha Aiyar's Law Lexicon 1997 edition at page 261, "bye-law" has been defined to include all orders, ordinances, regulations, rules and statutes made by any authority subordinate to the Legislature. The subordinate authority must, of course, have power

expressly or impliedly conferred on it to legislate on the matters to which the bye-law relates. At page 1697, of the same law dictionary "Rule" has been defined as "a prescribed, suggested or self imposed guide for conduct or action; a principle; a kind of regulation or bye-law: a principle regulating some action. In D.D.Basu's Administrative Law, 4th edition, 1996 at page 128 subordinate legislation has been referred to as including rules, bye-laws, regulations orders etc. Bye-law has been defined to mean bye-laws are rules made, in exercise of statutory power, by some authority, subordinate, to the Legislature (i.e. Municipal and other local bodies, public utility corporations, empowered by statute to make bye-laws), for the regulation, administration or management of some local area, property undertaking etc. which are binding on all persons who come within their scope."

Thus, from the above, we are of the view that the circular dated 30th May 2012 passed by the SEBI in exercise of its powers under Sections 11(1) and 11(2)(j) of the SEBI Act, 1992 read with Section 5 of the SCRA Act, 1956, which is the subject matter of challenge in this petition, could be termed as a statutory circular having a force of law and binding to all the Stock Exchanges in the country.

IX. Legality and validity of the regulations :

The following provisions of the regulations are challenged by the petitioners :

A. Section 2(r) (definition of Shareholders' Director) whereby he is denied voting right to elect Shareholders' Director.

B. Regulations 14(1) and 14(3) providing net worth for requirement of Rs.100/- crore.

C. Regulation 23(7) provides that no Trading Member or Clearing Member of their associates and agents shall be on the Governing Board on any recognized Stock Exchange or recognized Clearing Corporation.

The challenge to the regulation 2(r) and regulation 23(7) of Chapter V is to the following effect :

A. Vadodara Stock Exchange Corporation and Demutualization Scheme, 2005 is sanctioned by order under Section 4(B)(6) read with Section 4(B)(7) of the SCR Act and the regulations cannot modify the sanction Scheme.

B. 4.2 of the Scheme provides for representations of the Trading Members not to exceed one-fourth of the total strength of the Governing Board. Once the Scheme is

sanctioned, the SEBI is not competent to amend the Scheme.

The above takes us to the submission canvassed on behalf of the petitioners that after the approval of the Scheme under Section 4(B)(2) of the SCRA Act, 1956, the SEBI could not have imposed any new condition in the form of a circular, directing that if the Stock Exchange is not able to achieve the prescribed turnover of Rs.1000 crore on continuous basis or does not apply for voluntary surrender of recognition and exit before the expiry of two years from the date of the circular, it shall proceed with compulsory derecognition and exit of such Stock Exchanges in terms of the conditions as may be specified by the SEBI.

Mr.Thakore's submission in this regard is that when the Scheme is put forward for approval, at that point of time, after making necessary inquiry as may be necessary and after obtaining such further information, if any, and after being satisfied that it would be in the interest of the trade and also in the public interest, the SEBI may approve the Scheme with or without modification. Therefore, according to Mr.Thakore, if any modification is necessary in view of the SEBI, then it can

ask the Stock Exchange to make the necessary modification, but once the scheme is approved and made final, thereafter at a later stage, it cannot impose any further condition. In addition to this, according to Mr.Thakore, the SEBI, while approving the scheme under sub-section (2) of Section 4B, can restrict only three things as laid down under Section 4(B)(6)(a), (b) and (c).

We are not impressed even by this submission of Mr.Thakore. The schemes approved by the SEBI under Section 4(B) of the SCRA Act, 1956, do not restrain or denude the SEBI of the power to regulate the Stock Exchanges through other measures including by way of subordinate legislation or issuance of regulatory direction. Mr.Shelat, the learned advocate appearing for the SEBI, is justified in submitting that the power to regulate the Governing Board of Stock Exchanges does not solely flow from Section 4(B) of the Act, 1956. Such an interpretation would render all other provisions of the SCRA as well as the SEBI Act otiose. It is too much to say that a scheme once framed under Section 4(B) would be sacrosanct for all times to come without leaving any scope for the SEBI as a regulator to review the regulatory structure. In our opinion, the interpretation put forward on behalf of the petitioners

would defeat the purpose of regulatory powers conferred on the SEBI by the SCRA and the SEBI Act. Mr.Shelat is right in submitting that it is an on-going process. The proviso under sub-section (1) of Section 4B of the SCRA Act provides that exchanges, which were already corporatised and demutualised, do not have to submit a scheme for approval by the SEBI. If the submission of Mr.Thakore is accepted, it would mean that the SEBI would be powerless to further regulate those exchanges as regards its ownership and governance structure. While granting sanction under Section 4(B)(6) and 4(B)(7), it is specifically provided that sanction is conditional reserving right to amend, alter or modifying the Scheme is in the public interest and in furtherance of the objects of the Corporatisation and Demutualisation of the Stock Exchanges. Therefore, in view of clause (8) of the order, the SEBI is competent to impose further condition as regards voting rights of the Trading Members and deny voting rights to the Trading Members and deny right to vote for electing Shareholders' Director. The Scheme is incorporated in the Article of Association of the Stock Exchange. The Article of Association are rules within the meaning of Section 2(g) of the SCR Act, 1956. Under Section 7(A) recognized Stock Exchange has enabling power restricting voting rights (Articles of

Association). Under Section 8, the SEBI has power to direct modification of rules (Articles of Association). Under Section 12A of the Act, the SEBI can issue direction to secure proper management of the Stock Exchange. Therefore, there is ample power under the Act to make regulation. The Vadodara Stock Exchange is granted renewal every year, and while granting renewal, it is competent for the SEBI to provide further condition from time to time under Section 4 of the SCR Act read with rule 6 of 1957 Rules, and while seeking recognition, the Stock Exchange is required to give an undertaking to comply with other conditions and terms as may be imposed.

The scope of regulation 11(1) is sufficiently wide to meet situations, for which measures are not specifically provided in the regulation. Merely because in section 11(2) it is provided that "the measures referred to therein may provide for" cannot be taken to mean that such measures have to be laid down in advance. It is a matter of common knowledge that the SEBI has to regulate a speculative market and in case of speculative market varied situations may arise and all such exigencies and situations cannot be contemplated in advance and, therefore, looking to the exigencies and the requirement, it has been entrusted with the duty and function to take such measures as

it thinks fit. Instead of general principles of law, in such cases we have to consider the matter on first principle. The first principle is that the provisions of an Act have to be given a meaning so as to advance the object sought to be achieved by that Act. The duty and function had been entrusted to take such measures as it thinks fit and in order to discharge this duty the power is vested under section 11B. Thus, there is an authority under law to take the measures and merely because the measures have not been laid down in advance and published. It cannot be said that SEBI had no other authority under law to issue the directions, as contained in the impugned circular. The authority has been given under the law to take appropriate measures as it thinks fit and that by itself is sufficient to cloth the SEBI with the authority of law.

Section 11 and Section 11B are interconnected and coextensive as both these sections are mainly focused on investor protection. The SEBI has been in no uncertain terms mandated to protect the interests of investors in securities by such measures as it thinks fit, subject to the provisions of the Act. The expression 'measure' has not been defined in the Act. So we have to go by its generally understood meaning. According to Corpus Juris Secundum measure means “anything

desired or done with a view to the accomplishment of a purpose, a plan or course of action intended to obtain some object, any course of action proposed or adopted by a Government".

If the SEBI's powers to modify the scheme for individual Stock Exchanges under Section 4(B) is recognised, then as a measure of necessary corollary considering the SEBI's broad regulatory powers under the Act, it could be said that the SEBI also has power with regard to ownership and governance of all Stock Exchanges in general. Such power has been exercised by way of framing of the regulations. Such aspects of the ownership and governance that needed to be clarified by way of circulars, was done so, and accordingly, the impugned circular dated 13th December 2013 was issued.

It appears from the materials on record that the SECC Regulations as well as the impugned Exit Circular dated 30th May 2012 were issued by the SEBI after due consultation with all the stakeholders including the recognized Stock Exchanges although there is no such statutory mandate for the SEBI to make such consultations before framing the regulations or

issuing the circulars. The VSEL also had submitted its views on the Bimal Jalan Committee Report and the SMAC Committee decisions which were the basis on which the SECC Regulations and the Exit Circular were framed.

There is one another important aspect which needs to be noted and that is the Parliament has not treated the Stock Exchanges like any other public limited companies which are ordinarily governed in such matters exclusively by the provisions of the Companies Act. The Parliament has made special provisions for regulating the formation of the Stock Exchanges and also for their governance including the constitution of the Governing Board of the Stock Exchange. If the Stock Exchange were intended by the Parliament to be treated like any other public limited company, there was no need for the Parliament to make a special enactment like the Securities Act. Such is the reason why there is no violation of the Companies Act as contended.

Security Contract Regulation Act and the SEBI Act are special Acts and have an overriding effect over some of the provisions of the Companies Act. Section 616D of the Companies Act provides that the Companies Act shall apply to

any other company governed by the special Act except insofar as the said provisions are inconsistent with the provisions of such special Act. The SCR Act provides overriding effect to the following provisions :

(a) Section 8 provides for direction by the SEBI.

(b) The powers under Section 8 are delegated to the SEBI.

(c) Section 7A recognition Stock Exchange to make rules restricting voting rights.

(d) Section 4-B(6) provides that the SEBI is authorized to restrict the maximum number of representatives of the stock brokers on the Governing Board which shall not exceed one-fourth of the total strength of the Governing Board.

(e) Section 12-A(c) provides for direction by the SEBI for securing proper management of any Stock Exchange or Clearing House.

(f) Regulations framed under Section 31 of the Act are required to be laid before the Parliament and it becomes part of the statutory law.

Section 7A of the SCRA Act, 1956, makes it clear that the rules as approved by the Central Government shall be deemed to have been made validly notwithstanding anything contained to the contrary in the Companies Act, 1956.

The above takes us to consider the submission canvassed on behalf of the petitioners as regards the justification and the rationale in imposing the condition of turnover of Rs.1000 crore in the circular. According to the petitioners, there is no valid reason or rationale behind the regulations and the circulars. On the contrary, by imposing such a harsh condition, according to the petitioners, it virtually amounts to infringement of the right to trade as enshrined under Article 19(1)(g) of the Constitution of India.

We are not impressed even by this submission canvassed on behalf of the petitioners for the simple reason that there is no prohibition in the circular which prevents the petitioners from carrying on trade and earn livelihood as traders or brokers. However, we find it very difficult to accept the submissions of the petitioners that they have a fundamental right under Article 19(1)(g) of the Constitution of India to trade at a particular Stock Exchange only and that is the Vadodara

Stock Exchange.

So far as the imposition of the condition of turnover of Rs.1000 crore is concerned, we have made it very clear that it is not for this Court to comment on the economic policy of the SEBI.

In M/s. Shri Sitaram Sugar Co. Ltd. v. Union of India, AIR 1990 SC 1277, the Supreme Court observed in para 57 as under:-

> "*Judicial review is not concerned with matters of economic policy. The Court does not substitute its judgment for that of the legislature or its agents as to matters within the province of either. The Court does not supplant the "feel of the expert" by its own views..... Judicial inquiry is confined to the question whether the findings of fact are reasonably based on evidence and whether such findings are consistent with the laws of the land..... Price fixation is not within the province of the Courts. Judicial function in respect of such matters is exhausted when there is found to be a rational basis for the conclusions reached by the concerned authority.*"

In P.T.R. Exports (Madras) Pvt. Ltd. v. Union of India, AIR 1996 SC 3461, the Supreme Court observed in paras 3 and 5 as under :-

"The power to lay policy by executive decision or by legislation includes power to withdraw the same unless in the former case, it is by mala fide exercise of power or the decision or action taken is in abuse of power. The doctrine of legitimate expectation plays no role when the appropriate authority is empowered to take a decision by an executive policy or under law. The Court leaves the authority to decide its full range of choice within the executive or legislative power. In matters of economic policy, it is a settled law that the Court gives a large leeway to the executive and the legislature. ..... Government would take diverse factors for formulating the policy..... in the overall larger interest of the economy of the country. It is, therefore, by exercise of the power given to the executive or as the case may be, the legislature is at liberty to evolve such policies. A prior decision would not bind the Government for all times to come. When the Government is satisfied that change in the policy was necessary in the public interest, it would be entitled to revise the policy and lay down new policy. The Court, therefore, would prefer to allow free play to the Government to evolve fiscal policy in the public interest and to act upon the same."

In our opinion there should be judicial restraint in fiscal and economic regulatory measures. The State should not be hampered by the Court in such measures unless they are clearly illegal or unconstitutional. All administrative decisions in the economic and social spheres are essentially ad hoc and

experimental. Since economic matters are extremely complicated, this inevitably entails special treatment for distinct social phenomena. The State must therefore be left with wide latitude in devising ways and means of imposing fiscal or regulatory measures, and the Court should not, unless compelled by the statute or by the Constitution, encroach into this field.

We should not be understood to have meant that the judiciary should never interfere with administrative decisions. However, such interference should be only within the narrow limits e.g. when there is clear violation of the statute or a constitutional provision, or there is arbitrariness in the Wednesbury sense. It is the administrators and legislators who are entitled to frame policies and take such administrative decisions as they think necessary in the public interest. The Court should not ordinarily interfere with policy decisions, unless clearly illegal.

If, for non-fulfillment of the conditions imposed by the SEBI in its circular, the VSEL gets derecognized, then it cannot be said that with such derecognition the fundamental right of the petitioners to trade in shares at the VSEL would get infringed under Article 19(1)(g) of the Constitution of India. The fundamental rights guaranteed under Article 19 of the

Constitution of India are not absolute but the same are subject to reasonable restrictions to be imposed against the enjoyment of such rights. Such reasonable restrictions seek to strike a balance between the freedom guaranteed by any of the clauses under Article 19(1) and the social control permitted by the clauses (2) to (6) under Article 19 of the Constitution of India. As held by the Supreme Court in Krishnan Kakkanth v. Government of Kerala and others, AIR 1997 SC 128, that the reasonableness of restriction is to be determined in an objective manner and from the stand point of the interests of general public and not from the stand point of the interests of the persons upon whom the restrictions are imposed or upon abstract consideration. A restriction cannot be said to be unreasonable merely because in a given case, like in the present case, it operates harshly. In determining the infringement of the right guaranteed under Article 19(1) of the Constitution of India, the nature of right alleged to have been infringed, the underlying purpose of the restriction imposed, the extent and urgency of the evil sought to be remedied thereby, the disproportion of the imposition, the prevailing conditions at the time, enter into judicial verdict. Therefore, although a citizen has a fundamental right to carry on a trade or business, yet he has no fundamental right to insist upon the

State that he will carry on trade or business only at the Vadodara Stock Exchange.

In the aforesaid context, we may quote the observations of the Supreme Court as contained in paras 32 and 34 of Krishnan Kakkanth (*supra*) as under :

> *"32. It has already been indicated that in Vikalad's case (AIR 1984 SC 95) (supra), it has been held by this Court that infringement of fundamental right under Article 19(1)(g) must have a direct impact on the restriction on the freedom to carry on trade and not ancillary or incidental effects on such freedom to trade arising out of any governmental action.It has also been held in that case that unless the trader or merchant is not wholly denied to carry on his trade, the restriction imposed in denying the allotment of wagon in favour of such trader or merchant to transport coal for carrying out trading activities does not offend Article 19(1)(g) of the Constitution. No restriction has been imposed on the trading activity of dealers in pumpsets in the state of Kerala including northern region comprising eight districts. Even in such area, a dealer is free to carry on his business. Such dealer, even in the absence of the said circular, cannot claim as a matter of fundamental right guaranteed under Article 19(1)(g) that a farmer or agriculturist must enter into a business deal with such trader in the matter of purchase of pumpsets. Similarly,*

such trader also cannot claim that the Government should also accept him as an approved dealer of the Government. The trading activity in dealership of pumpsets has not been stopped or even controlled or regulated generally. The dealer can deal with purchasers of pumpsets without any control imposed on it to carry on such business. The obligation to purchase from approved dealer has been fastened only to such farmer or agriculturist who has volunteered to accept financial assistance under the scheme on various terms and conditions."

"34.To ascertain unreasonableness and arbitrariness in the context of Article 14 of the Constitution, it is not necessary to enter upon any exercise for finding out the wisdom in the policy decision of the State Government. It is immaterial if a better or more comprehensive policy decision should have been taken. It is equally immaterial if it can be demonstrated that the policy decision is unwise and is likely to defeat the purpose for which such decision has been taken. Unless the policy decision is demonstrably capricious or arbitrary and not informed by any reason whatsoever or it suffers from the vice of discrimination or infringes any statute or provisions of the Constitution, the policy decision cannot be struck down. It should be borne in mind that except for the limited purpose of testing a public policy in the context of illegality and unconstitutionality, Court should avoid "embarking on uncharted ocean of public policy"."

Mr.Thakore very strenuously contended that it is only the Central Government who is empowered to impose the conditions under Section 30 of the Act, 1956 and not the SEBI. Mr.Thakore submitted that assuming for the moment that the SEBI is empowered to impose such conditions, then it can do so only after regard to the following :

(1) After consultation with the Governing Board of the Stock Exchange;

(2) Having regard to the area served by the Stock Exchange; and

(3) Its standing and the nature of the securities dealt with by it.

Such contention of Mr.Thakore flows from the provision of Section 4(1)(b). We are afraid, we are not impressed by such submission of Mr.Thakore as this issue is no longer *res integra* after the pronouncement of the decision of the Supreme Court in the case of Madhubhai Amathalal Gandhi (*supra*).

In the case before the Supreme Court, condition 2(i)(a) was imposed, which provided that the members of the Indian Stock Exchange Limited, Bombay, would be entitled to apply for membership of the Stock Exchange, Bombay, provided they

fulfill or comply with certain terms and conditions. The contention before the Supreme Court was that condition 2(i)(a) enabled only the active members of the Indian Stock Exchange Limited to apply for membership of the Stock Exchange, Bombay, and such condition could be imposed only if it amounts to a qualification of membership within the meaning of sub-section (2) of Section 4. Repelling such argument, the Supreme Court observed the following :

> *“...The argument proceeds that condition 2(i)(a) enables only the active members of the Indian Stock Exchange Limited to apply for membership of the Stock Exchange, Bombay and that such a condition can be imposed only if it amounts to a qualification of membership within the meaning of sub-s. (2) of s. 4, as the other conditions in that sub-section are obviously inapplicable. It is further pointed out that sub- s. (2) refers back to sub-s.(i)(a) and under that clause the condition imposed must only be that prescribed by the Rules made under the Act and that the condition imposed by the notification is not a condition so prescribed. There is force in this argument; but, the acceptance of this contention does not advance the case of the petitioner, for, if the condition is not covered by cl. (a) of s. 4(1), it falls under cl. (b) thereof. Under that clause, the Central Government may grant recognition to a Stock Exchange if the said Stock Exchange is willing to comply with " any other conditions ". It is said that the other conditions in s. 4 (1) (b) must*

only be conditions relating to the area served by the Stock Exchange, its standing and the nature of the securities dealt with by it. This is not what cl. (b) of s. 4(1) says. The conditions under cl. (b) of s. 4(1) no doubt shall be such as may be imposed by the Government, having regard to the aforesaid three considerations, but they need not necessarily be confined only to the said considerations. The Government may impose any conditions, no doubt germane to the recognition of a Stock Exchange, after consultation with its governing board, and having regard to the said considerations."

"...The condition is, germane to the recognition of Stock Exchange and is, therefore, a condition within the meaning of 'any other conditions' in Cl.(b) of sub-s.(1) of S.4 of the Act."

Therefore, once it is found that the condition is, germane to the recognition of the Stock Exchange, then such a condition would fall within the meaning of 'any other conditions' in Clause (b) of sub-section (1) of Section 4 of the Act.

Mr.Thakore further submitted that on the plain reading of Section 4B(6)(c), it suggests the number of Directors of the share brokers group. To put it in other words, it contemplates a representation on the Governing Board. Section 4B(6)(c) of the Act, 1956, empowers the SEBI while approving the scheme to

provide for the maximum number of representations of the stock brokers of the recognised Stock Exchange to be appointed on the Governing Board which shall not exceed one-fourth of the total strength of the Governing Board. The words 'not exceeding' provided for the maximum number of stock brokers to be appointed on the Governing Board. The minimum could be zero also.

Mr.Shelat, the learned senior advocate appearing for the SEBI, in this context has placed reliance on the term 'not exceeding' as explained in Stroud's Judicial Dictionary of Words and Phrases, Sixth Edition. It reads as under :

> *“A sum 'not exceeding' : see per Bayley J., Cortis v. Kent Water Works Co., 7 B. & C. 340; Palmer v. Newell [1872] W.N. 9; see further R. v. St.George's Southwark, 19 Q.B.D. 533. In Cortis v. Kent Water Works Co., 7 B. & C. 314, the phrase was held, under the circumstances, as connoting a minimum.”*

> *“Not more than [S.154 IPC (45 of 1860)]; [S.57(a)(2), TP Act (4 of 1882)].”*

In our opinion, the words 'not exceeding' means that it confers upon the SEBI the discretion to determine the number

of stock brokers on the Governing Board. However, in this regard, Mr.Shelat submitted that the words 'not exceeding' could also mean zero number of brokers on the Governing Board.

The denial of right to be on the Board of Management and/or denial of right to vote for Shareholders' Director is because with the experience gained it has been found by the SEBI that there is total conflict of interest if the Trading Members are on the Board of Directors. It was found that the Trading Members were influencing the decision making process. The importance of the net worth has been explained in the Bimal Jalan Report. Even as a shareholder, the petitioners' other rights are protected. The petitioners have a right to attend the General Meeting, Special Meeting, and by majority, can participate in the decision making policy at the General Board. The Directors are not within the control of the SEBI, as is alleged. The Public Interest Directors are independent Directors and it is erroneous to suggest that only the Trading Members can alone provide for greater turnover and/or net worth.

For the foregoing reasons, we do not find any merit in

any of the submissions canvassed on behalf of the petitioners. We are of the view that the petitioners are not entitled to any of the reliefs as prayed for in the petition. Resultantly, the petition fails and is hereby dismissed. However, in the facts and circumstances of the case, there shall be no order as to costs.

The Writ Petition (PIL) No.211 of 2012 has been filed in public interest by the Chairman of the Investor's Protection, Education and Research Centre, challenging the same circular which is the subject matter of adjudication in the main Special Civil Application, which we have ordered to be dismissed. As the issues raised in the writ petition filed in public interest are the same and as we have dismissed the Special Civil Application No.17040 of 2012, this writ petition also fails and is hereby rejected. However, in the facts and circumstances of the case, there shall be no order as to costs.

(BHASKAR BHATTACHARYA, CJ.)

(J.B.PARDIWALA, J.)

MOIN