

THE SECURITIES CONTRACTS (REGULATION) ACT, 1956

Question 1

- (a) (i) *Delhi Stock Exchange wants to establish additional Trading Floor. Explain briefly the meaning of and procedure for establishing additional Trading Floor.*
- (ii) *Complaints of unethical practices have been received against members of the Governing Body of a Recognized Stock Exchange. Examine whether the Government has any power to take action against the Governing Body of the said exchange.*
- (b) *The application filed by M/s XYZ Ltd. for the listing of its securities has been rejected by the Mumbai Stock Exchange. Advise the company regarding the steps it can take against the rejection.* **(November, 2002)**

Answer

- (a) (i) According to Section 13 A of Securities Contracts (Regulation) Act 1956, a Stock Exchange may establish additional trading floor with the prior approval of the Securities Exchange Board of India in accordance with the terms and conditions stipulated by the said Board.
- For the purpose of this section 'Additional Trading Floor' means a trading ring or trading facility offered by a recognized stock exchange outside its area of operation to enable the investor to buy and sell securities through such trading floor under the regulatory frame work of that Stock Exchange.
- (ii) Section 11, of the Securities Contracts (Regulation) Act, 1956 deals with the powers of the Central Government to supersede the Governing body of a recognized Stock Exchange. The Central Government may serve on a governing body a written notice specifying the reasons and after giving an opportunity to the governing body to be heard, may, by notification in the Official Gazette, declare the governing body as superseded. The Central Government after superseding the governing body may appoint any person or persons to exercise and perform all the powers and duties of governing body. It may also appoint one of such nominees as Chairman.

- (b) Yes XYZ Ltd. can appeal against refusal of stock exchange to list the securities. Section 22 of Securities Contracts (Regulation) Act 1956 deals with this. According to section:

where a recognized stock exchange refuses listing to a company, it has to furnish reasons for refusal to the company. Section 73(1) of the Companies Act, 1956 specifies the time period within which stock exchange has to grant listing permission. If exchange fails to do so within the time limit or refuses to list, the company may within 15 days make an appeal to the Central Government. The Central Government may after hearing the Stock Exchange vary or set aside the decision of the Stock Exchange, or grant permission for listing.

However, no appeal under this section shall be allowed after the commencement of Securities Laws (Second Amendment) Act 1999 since appeal before Securities Appellate Tribunal is permitted under Section 22A.

Where a Stock Exchange refuses listing or is unable to grant listing within time frame prescribed, company is entitled to appeal to Securities Appellate Tribunal (SAT). SAT may, after hearing the exchange vary or set aside exchange's order or grant or refuse. (Section 22A).

Question 2

- (a) *M/s AB & Company, a member of a recognised stock exchange propose to buy and sell shares of a particular company on behalf of investors as well as on their own account. They seek your advice as to restrictions, if any, under Securities Contracts (Regulation) Act, 1956 for dealing in securities on their own account. Advise.*
- (b) *Rampur Stock Exchange wants to get itself recognize. Explain':*
- (i) *Who enjoys the power to recognize stock exchange?*
- (ii) *What information will have to be provided with the application for recognition?*

(May, 2003)

Answer

- (a) **Members not to act as principals in certain circumstances:**

Members of stock exchange normally carry out transactions on behalf of investors and hence principal agent relationship exists. A Member can enter into transaction as principal with another member of the Exchange only. If he desires to enter into contract as principal with a non-member, then he has to get written consent from such person to act as principal. Contract note should indicate that he is acting as principal [Section 15, Securities Contract (Regulation) Act, 1956].

Where the member has secured the consent of such person other wise than on writing he shall secure written confirmation by such person or such consent within three days from the date of the contract [Proviso to Section 15].

Spot delivery contracts are outside the preview of section 15 (Section 18).

A & Co, stock broker must bear in mind the above restrictions while entering into any transaction as principal with a non member.

- (b) (i) Power to recognize Stock Exchange vests with Central Government. However, Central Government has delegated the powers to SEBI vide its notification No.F.No.1/57/SE/93 dated 13.9.94. (Section 3 of Securities Contracts (Regulation) Act, 1956).
- (ii) Application for recognition must be accompanied with Bye-Laws, Rules, Regulations which must contain specific details on:
 - 1. Constitution, powers of management and manner of transacting business by the Governing Body of the Stock Exchange.
 - 2. Powers and duties of the offer bearers of Stock Exchange.
 - 3. Various classes of Members, qualification of membership and the exclusion, suspension, expulsion and re-admission of members.
 - 4. The procedure for registration of Partnerships as members to stock exchange and rules of nomination of authorised representatives.

Membership provisions, composition of Board Powers of Governing Board are defined in the Articles of the Exchange. Rules governing Listing Trading and Settlement, Penalties and Prohibitions, Disciplinary Actions and Defaults are defined in Bye-Laws of the Exchange.

Question 3

- (a) *Mr. Patel has transferred his shares of a listed company registered in his name to Mr. Mehta. Mr. Mehta has failed to get the shares registered in his name before the company declared and paid the dividend on the shares. Examine with reference to the provisions of Securities Contracts (Regulation) Act, 1956 whether Mr. Patel is entitled to retain the dividend even though he has transferred the shares before declaration of dividend.*
- (b) *SEBI is of the opinion that in the interest of investors it is desirable to amend the rules of XYZ Stock Exchange prohibiting the appointment of the broker-member as President of the stock exchange. Explain with reference to the provisions of the Securities Contracts (Regulation) Act, 1956 whether it is possible for SEBI to amend the rules of the Stock Exchange, if the rules are not amended by the stock exchange.*

(November, 2003)

Answer

- (a) **Title to dividends:** Section 27(1) of Securities Contracts (Regulation) Act, 1956 provides that a holder of security can legally receive and retain any dividend declared by the company even if he has transferred the security for valuable consideration. However, he (i.e. holder of security who is a transferor) cannot receive or retain the dividend if the transfer deed with all other documents required for transfer are lodged with the company within 15 days of the date on which the dividend became due.

The period of 15 days shall be extended as follows: - (1) In case of death of the transferee by the actual period taken by his legal representative to establish his claim to the dividend. (2) In case of loss of the transfer deed by theft or any other cause beyond the control of the transferee, by the actual period taken for the replacement thereof and (3) In case of delay in the lodging of any security and other documents relating to the transfer due to causes connected with the post, by the actual period of delay (Explanation to Section 27(1) of SCRA).

In view of the above, Mr. Patel is entitled to retain the dividend received by him if the transferee, Mr. Mehta has not lodged the transfer deed with the company within 15 days of the date on which the dividend became due or the extended period as per explanation to Section 27(1).

However, Section 27(1) will not affect the right of the transferee to enforce his rights, if any against the transferor or any other person, if the company refuses to register the transfer of security in the name of the transferee.

- (b) **Power of Central Government/SEBI to direct rules to be made or to make rules:** Central Government is empowered under Section 8 of the Securities Contracts (Regulation) Act, 1956 to issue written order directing all or any of the recognized stock exchanges to make any rules or to amend any rules already made within 2 months from the date of the order in respect of matters specified in Section 3(2). One of the matters specified in Section 3(2) is the governing body of stock exchange, its constitution and powers of management and the manner in which its business is to be transacted. Hence, the Central Government is empowered to direct the Stock Exchange in respect of prohibition of broker-member being appointed as president of the stock exchange. According to the notification issued by the Central Government under Section 29A, this power is also exercisable by SEBI.

If any recognized stock exchange fails or neglects to comply with any order made by SEBI within 2 months, SEBI may itself make the rules made, either in the form prepared in the order or with such modifications thereof as may be agreed to between the stock exchange and SEBI. The amended rules should be published in the Gazette of India and also in the Official Gazette of the State in which the principal office of the

recognized stock exchange is situated. After such publication, the rules will be valid, as if they had been made or amended by the stock exchange itself.

Hence SEBI can issue directions to the recognized stock exchange to amend the rules and if the said stock exchange does not take steps for amending the rules, SEBI may amend the rules on its own by following the procedure laid down in Section 8.

Question 4

- (a) *Securities and Exchange Board of India received serious complaints against the Affairs of a Member of a Stock Exchange. Explain the powers of SEBI under Securities Contracts (Regulation) Act, 1956 to make enquiries and to take action, if necessary, against the member of a Stock Exchange.*
- (b) *The governing body of City Stock Exchange Association Ltd. is desirous of putting various restrictions on voting rights of its members to be exercised in a meeting and on their right to appoint a proxy. You are required to state whether the same is permissible. Also state the role of Central Government in this respect. (May, 2004)*

Answer

- (a) **Disciplinary action against members of Stock Exchange:** SEBI can exercise the following powers under Securities Contracts (Regulation) Act, 1956 on receipt of serious complaints against the affairs of a member of a stock exchange.
- (i) SEBI may, if it is satisfied that it is in the interest of the trade or in the public interest, by order in writing call upon the member of the stock exchange to furnish in writing information or explanation in respect of the matter under inquiry [Section 6(3)(a)].
- (ii) SEBI instead of calling for information, may either appoint one or more persons to make an enquiry or direct the governing body of stock exchange to make inquiry and submit its report to SEBI [Section 6(3)(b)].

In case of adverse findings, SEBI can direct stock exchange to take disciplinary action against the member such as fine, expulsion from membership, suspension from membership for a specified period and any other penalty of a like nature not involving the payment of money. Bye-laws of the stock exchange usually provide for such punishment [Section 9(3)(b)]. Stock exchange is under obligation to take the action as directed.

- (b) As per Section 7A(1) of the Securities Contracts (Regulation) Act, 1956 a recognized stock exchange may make rules or amend any rules made by it in respect of voting rights of its members and also on appointment of proxy. The restrictions can be put in respect of the following matters:

- (a) The restriction of voting rights to the members only in respect of any matter placed before the stock exchange at any meeting.
- (b) The regulation of any voting rights in respect of any matter placed before the stock exchange at any meeting so that each member may be entitled to have one vote only, irrespective of his share of the paid up equity capital of the stock exchange.
- (c) The restriction on the right of a member to appoint another person as his proxy to attend and vote at a meeting of the stock exchange.
- (d) Such incidental, consequential and supplementary matters as may be necessary to give effect to the matters as stated in (a), (b) and /or (c) above.

As per section 7(A)(2) of the said Act, the role of the Central Government in respect of the restriction placed by the stock exchange as stated above is as follows:

- (i) Approval of the proposed changes by the stock exchange.
- (ii) Publishing the same in the Official Gazette.
- (iii) To make such modification in the proposed changes as it deems fit.

Question 5

The Rural Electrification Corporation, New Delhi issued 6 years bonds to public directly and not through any Stock Exchange. Whether the Rural Electrification Corporation can do so? Is it not a violation of Securities Contracts (Regulation) Act, 1956? (November, 2004)

Answer

In order to prevent undesirable transactions in securities and to promote healthy stock market, the Securities Contract (Regulation) Act, 1956 was enacted. Stock Exchanges are recognized under the Act. Section 73 of the Companies Act, 1956 lays down that offer of shares or debentures to public for subscription shall be only after the permission of the Stock Exchange. Section 28 of the Securities Contract (Regulation) Act, 1956 says that the provisions of the Act shall not apply to the Government, the Reserve Bank of India, any local authority or any corporation set-up by a special law or any person who has effected any transaction with or through the agency of any such authority as stated above. The Rural Electrification Corporation is a corporation established under a special statute enacted by the Parliament. Therefore, the Corporation need not require permission of any Stock Exchange. It is exempted. There is no violation of the provisions of the Act of 1956 because according to section 28 provisions are not applicable to this corporation.

Question 6

Working of City Stock Exchange Association Ltd., is not being carried on by its Governing Board in public interest. On receipt of representations from various Investors and Investors'

The Securities Contracts (Regulation) Act, 1956

Association, the Central Government is thinking to withdraw the recognition granted to the said Stock Exchange. You are required to state the circumstances and procedure for withdrawal of such recognition as per the provisions of Securities Contracts (Regulation) Act, 1956 in this regard. Also state the effect of such withdrawal on the contracts outstanding on the date of withdrawal.
(May 2005)

Answer

Section 5 of the Securities Contracts (Regulation) Act, 1956 empowers the Central government to withdraw the recognition granted to a Stock Exchange. The circumstances and procedure to be followed for withdrawal of such recognition is stated below:

- (i) If, considering the interest of the trade or the public interest, the Central Government is of the opinion that the recognition granted to a stock exchange should be withdrawn, the Central Government shall serve a written notice of the governing body of the stock exchange.
- (ii) The said notice shall specify the reasons for the proposed withdrawal of the recognition.
- (iii) The governing body of the stock exchange shall be afforded an opportunity of being heard by the Central Government.
- (iv) Even after hearing the governing body, the Central Government is satisfied that the recognition granted to the stock exchange should be withdrawn, the Central Government may, by way of a notification in the Official Gazette, withdraw the recognition granted to the stock exchange.

The proviso to the said section 5 states that no such withdrawal shall affect the validity of any contract entered into or made prior to the date of notification withdrawing the recognition 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 for the due performance of any contracts outstanding on that date.

Question 7

Delhi Stock Exchange has refused to grant listing of the shares of ABC Limited but the Exchange has not disclosed any reason therefore. The company wants to challenge the decision of the Stock Exchange in the Civil Court.

Advise the company pursuant to relevant provisions of the Securities Contracts (Regulation) Act, 1956.
(May 2005)

Answer

Under section 22A of the Securities Contracts (Regulation) Act, 1956 where a recognised Stock Exchange refuses to list the securities of any public company, the company shall be entitled to be furnished with reasons for such refusal. If aggrieved, the company may appeal to the Securities Appellate Tribunal:

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- (i) within 15 days from the date on which the reasons for such refusal are furnished to it, or
- (ii) where the Stock Exchange has omitted or failed to dispose of within the time specified in section 73(1A) of the Companies Act, 1956 (i.e., before the expiry of ten weeks from the date of closing of the subscription list as per prospectus) within 15 days from the expiry of the specified time or within such further period not exceeding one month as Securities Appellate Tribunal may allow.

In terms of section 22E of the Act, Civil Court has no jurisdiction to entertain any suit in respect of this matter.

The company may be advised accordingly.

Question 8

Describe the provisions of the Securities Contracts (Regulation) Act, 1956 regarding the powers of the Central Government to supersede the Governing Body of a recognized Stock Exchange and the consequences of such supersession. (November 2005)

Answer

According to the provisions of section 11 of the Securities Contracts (Regulation) Act, 1956, where the Central Government is of opinion that the governing body of any recognized stock exchange should be superseded, then notwithstanding any thing contained in any other law for the time being in force, the Central Government may serve on the governing body a written notice that the Central Government is considering the supersession of the governing body for the reasons specified in the notice. After giving an opportunity to the governing body of such Stock Exchange to be heard in the matter, the Central Government may, by notification in the Official Gazette, declare the governing body of such Stock Exchange to be superseded.

The Central Government may appoint any person or persons to exercise and perform all the powers and duties of the governing body. If more than one person is so appointed, one of them may be the Chairman and another as the Vice-Chairman. Such person or persons shall hold office for such period as may be specified in the Notification and the Central Government may vary such period by way of another Notification.

On the publication of the notification in the Official Gazette, following are the consequences:

- (i) The members of the governing body of such Stock Exchange ceases to hold office as such members on and from the date of notification.
- (ii) The person or persons appointed by the Central Government may exercise and perform all the powers and duties of the governing body which has been so superseded.

- (iii) The property of the Stock Exchange as deemed necessary and so specified in writing by such person or persons to carry on the business of the Stock Exchange shall vest in such person or persons.

Question 9

- (i) *Delhi Stock Exchange wants to establish additional trading floor. Advise.*
- (ii) *Complaints of unethical practices have been received against members of a recognized Stock Exchange by the Government. Examine whether the government has any power to suspend the business of such a recognized Stock Exchange. (November 2005)*

Answer

- (i) According to Section 13A of Securities Contracts (Regulation) Act, 1956, a Stock Exchange may establish additional trading floor with the prior approval of the Securities Exchange Board of India with the terms and conditions stipulated by the said Board. 'Additional Trading Floor' means a trading facility offered by a recognized stock exchange outside its area of operation to enable the investors to buy and sell securities through such trading floor under the regulatory frame work of that Stock-Exchange.
- (ii) Section 12 of the Securities Contracts (Regulation) Act, 1956 deals with the powers of the Central Government to suspend business of recognized Stock Exchange. Central Government, if it deems fit, is vested with power to suspend business for a period not exceeding 7 days by notification in Gazette. Central Government also have power to extend this period by a like notification. However, such power can be exercised by the Central Government, if it is of opinion that an emergency has arisen and it is expedient so to do.

Question 10

On 31st March, 2006 D holds certain securities issued under 'Collective Investment Scheme.' His name appears in the books of the scheme. He has transferred these securities to another person for a consideration. The transferee lodged the instrument of transfer with the authorities one month after the date on which the income on these securities became due. Examining the provisions of the Securities Contracts (Regulation) Act, 1956 state:

- (i) *Whether D is entitled to receive and retain the income on these securities for the financial year ended 31st March, 2006 in the given case?*
- (ii) *Would your answer be still the same in case the transferee lodged the instrument of transfer with the authorities 14 days after the date on which the income on these securities became due? (May 2006)*

Answer

Transfer of securities under Collective Investment Scheme under the Securities Contracts (Regulation) Act, 1956 (Section 27A)

Problem as asked in the question is based on the provisions of Section 27A of the Securities Contracts (Regulation) Act, 1956, wherein it shall be lawful for the holder of any securities, being units or the other instruments issued by collective investment scheme, whose name appears on the books of the scheme, issuing the said security to receive and retain any income in respect of units issued by the scheme in respect thereof for any year, notwithstanding that the said security, being units issued by the scheme, has already been transferred by him for consideration, unless the transferee who claims the income in respect of units issued by the scheme from the transferor has lodged the security and all other documents relating to the transfer which may be required by the scheme with the scheme for being registered in his name within 15 days of the date on which the income in respect of units or other instruments issued under the scheme became due. The period of 15 days can be extended in certain contingencies as stated in Explanation to Section 27A(1).

Applying the above provisions in the given case:

- (i) the holder of securities (i.e. D, the transferor) has right to receive or retain the income on these securities for the financial year ended 31st March, 2006, since the instrument for transfer was lodged one month after the date on which the income became due.
- (ii) The answer in the second case would differ. The holder (i.e. D, the transferor) cannot receive and retain the income since the instruments for transfer was lodged with the company within the statutory period of 15 days by the transferee.

Question 11

The Executive Committee of a recognized Stock Exchange desires to transfer certain duties and functions of a clearing house to a recently set up Clearing Corporation, incorporated as a company under the Companies Act, 1956. Examining the provisions of the Securities Contracts (Regulation) Act, 1956:

- (i) *State the purpose for which such transfer of duties and functions can be made to Clearing Corporation.*
- (ii) *What is the procedure to be adopted for such transfer of duties and functions?*

(May 2006)

Answer

Transfer of certain duties and functions of a clearing house by a stock exchange to clearing corporation under the Securities Contracts (Regulation) Act, 1956 (Section 8A)

Purposes:

A recognized stock exchange may, with the prior approval of the Securities and Exchange Board of India, transfer the duties and functions of a clearing house to a clearing corporation, being a company incorporated under the Companies Act, 1956 for the purpose of:

- (i) the periodical settlement of contracts and differences thereunder,
- (ii) the delivery of, and payments for, securities;
- (iii) any other matter incidental to, or connected with, such transfer.

Procedure:

1. Every clearing corporation shall for the purpose of transfer of the duties and functions of a clearing house to clearing corporation make bye-laws and submit the same to the SEBI for approval.
2. The SEBI may, on being satisfied that it is in the interest of the trade and also in the public interest to transfer the duties and functions of a clearing house to a clearing corporation, grant approval to the bye-laws submitted to it under sub-section (2) and approve transfer of the duties and functions of a clearing house to a clearing corporation.
3. The provisions of Sections 4 to 12 shall, as far as may be, apply to a clearing corporation as they apply in relation to a recognized stock exchange.

Question 12

The shares of MLM Ltd. were listed in Cochin Stock Exchange. The stock exchange delists the shares of the company. The aggrieved company approaches you to know the remedy available to the company. Give your suggestion to the company keeping in view the provision of the Securities Contracts (Regulation) Act, 1956. (November 2006)

Answer

Section 21A of Securities Contracts (Regulation) Act, 1956 contains the provision relating to delisting of securities. As per this section

- (1) A recognized Stock Exchange may delist the securities after recording reasons therefor from any recognized stock exchange on any ground or grounds as may be prescribed under this Act.
- (2) The Securities of a company shall not be delisted unless the company concerned has been given a reasonable opportunity of being heard.
- (3) A listed company may file an appeal before the Securities Appellate Tribunal (SAT) against the decision of the recognized stock exchange delisting the securities within

fifteen days from the date of the decision of recognized stock exchange delisting the securities.

- (4) Securities Appellate Tribunal may, if it is satisfied that the company was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period of not exceeding one month.

So here, the company may make an appeal to the Securities Appellate Tribunal against the delisting within fifteen days or such extended period not exceeding one month after showing sufficient cause of not filing within fifteen days.

Question 13

Explain the powers, which can be exercised by the Securities and Exchange Board of India under the Securities Contracts (Regulation) Act, 1956, while approving the schemes for corporatisation and demutualization submitted by recognized stock exchanges, so that there is segregation of ownership and management from the trading rights of members of such stock exchanges.
(November 2006)

Answer

Corporatisation and Demutualisation – Power of SEBI under SCRA, 1956

SEBI has been empowered under sub-section (2) of Section 4B of Securities Contracts (Regulation) Act, 1956 to approve the scheme of corporatisation and demutualisation with or without modification. SEBI can reject the proposed scheme if it is satisfied that it would not be in the interest of the trade and also in the public interest to approve the scheme. Besides these general powers, SEBI has got certain specific powers under Section 4B(6). SEBI, while approving the scheme, may, by an order in writing restrict

- (a) the voting rights of the shareholders who are also stock-brokers of the recognized stock exchange.
- (b) the right of shareholders in a stockbroker of the recognized stock exchange to appoint the representatives on the governing board of the stock exchange.
- (c) the maximum number of representatives of the stock-broker of the recognized stock exchange to be appointed on the governing board of the stock exchange shall not exceed one-fourth of the total strength of the governing body.

On receipt of approval of scheme, stock exchange will issue shares to public within 12 months so that at least 51% equity shares are with public other than shareholders having trading rights. SEBI can extend the period upto another 12 months [Section 4B(8)].

Question 14

Describe the provisions of the Securities Contracts (Regulation) Act, 1956 regarding the powers of the Central Government to supersede the Governing Body of a recognized Stock Exchange and the consequences of such supersession.
(May 2007)

Answer

In accordance with the provisions of Section 11 of the Securities Contracts (Regulation) Act, 1956, where the Central Government is of opinion that the governing body of any recognized stock exchange should be superseded, then notwithstanding anything contained in any other law for the time being in force, the Central Government may serve on the governing body a written notice that the Central Government is considering the supersession of the governing body for the reasons specified in the notice. After giving an opportunity to the governing body of such Stock Exchange to be heard in the matter, the Central Government may, by notification in the Official Gazette, declare the governing body of such Stock Exchange to be superseded.

The Central Government may appoint any person or persons to exercise and perform all the powers and duties of the governing body. If more than one person is so appointed, one of them may be the Chairman and another as the Vice-chairman. Such person shall hold office for such period as may be specified in the Notification and the Central Government may vary such period by way of another Notification.

On the publication of the notification in the Official Gazette, following are the consequences:

- (i) the members of the governing body of such Stock Exchange ceases to hold office as such members on and from the date of notification.
- (ii) The person or persons appointed by the Central Government may exercise and perform all the powers and duties of the governing body which has been so superseded.
- (iii) The property of the Stock Exchange as deemed necessary and so specified in writing by such person or persons to carry on the business of Stock Exchange shall vest in such person or persons.

Question 15

SEBI is of the opinion that in the interest of investors, it is desirable to amend the rules of RSP Stock Exchange prohibiting the appointment of the broker-member as President of the Stock Exchange. Explain briefly with reference to the provisions of Securities Contracts (Regulation) Act, 1956, whether it is possible for SEBI to amend the rules of the Stock Exchange, if the Stock Exchange does not change the rules. **(May 2007)**

Answer

In accordance with the provisions of section 8 of Securities Contracts (Regulation) Act, 1956, The Central Government is empowered to issue written order directing all or any of the recognized stock exchange to make any rules or to amend any rules already made within two months from the date of the order in respect of matters specified in section 3(2) of the said Act. One of the matters specified in the said section 3(2) is the governing body of stock

exchange, its constitution and powers of management and the manner in which its business is to be transacted. Hence, the Central Government is empowered to direct the stock exchange in respect of prohibition on broker-member being appointed as President of the stock exchange. According to notification issued by Central Government under section 29A of the said Act, this power is also exercisable by SEBI.

If any recognized stock exchange fails or neglects to comply with any order made by SEBI within two months, SEBI may itself make the rules or amend the rules made by stock exchange either in the form proposed in the order or with such modification thereof as may be agreed to between SEBI and the stock exchange. The amended rules are required to be notified in the Gazette of India and in the Gazette of the State where the principal office of the stock exchange is situated. After such publication, the rules shall be valid as if the same were made or amended by the recognized stock exchange itself.

Accordingly of the above provisions of Securities Contracts (Regulation) Act, 1956, SEBI can issue directions to RSP Stock Exchange to amend the rules and if the said stock exchange does not comply with the above, SEBI can amend the rules on its own.

Question 16

PQR Ltd. is holding 33% of the paid up equity capital of Koya Stock Exchange. The company appoints MNL Ltd. as its proxy who is not a member of the Koya Stock Exchange, to attend the vote at the meeting of the stock exchange. Examine whether the Koya Stock Exchange can restrict the appointment of MNL Ltd. as proxy for PQR Ltd. and further restrict, the voting rights of PQR Ltd. in the Koya Stock Exchange. **(November 2007)**

Answer

Section 7(a) of the Securities (Contracts) Regulation Act, 1956 provides that a recognised stock exchange is empowered to amend rules to provide for all or any of the following matters:

- (a) Restriction of voting right to members only.
- (b) Regulation of voting rights by specifying that each member is entitled to one vote only irrespective of number of shares held.
- (c) Restriction on right of members to appoint proxy.

As such Koya Stock Exchange can restrict the appointment of MNL Ltd., as proxy, if rules of the exchange so provide. If it is not so provided, rules may be amended and after getting approval of the Central Government regarding amendment, it can restrict appointment of proxies.

Koya Stock Exchange can also restrict the voting rights of PQR Ltd. as proxy if rules of the exchange so provide. If it is not so provided, rules may be amended and after getting approval of Central Government regarding amendment, it can restrict appointment of proxies.

Koya Stock Exchange can also restrict the voting rights of PQR Ltd.

Question 17

Working of City Stock Exchange Association Ltd., is not being carried on by its governing Board in public interest. On receipt of representations from various investors and Investors' Association, the Central government is thinking to withdraw the recognition granted to the said Stock Exchange. You are required to state the circumstances the procedure for withdrawal of such recognition as per the provisions of Securities Contracts (Regulation) Act, 1956 in this regard. Also state the effect of such withdrawal on the contracts outstanding on the date of withdrawal. **(May 2008)**

Answer

Section 5 of the Securities Contracts (Regulation) Act, 1956 empowers the Central Government to withdraw the recognition granted to a stock exchange. The circumstances and procedure to be followed for withdrawal of such recognition is stated below

- (i) if considering the interest of the trade or the public interest, the Central government is of the opinion that the recognition granted to a stock exchange should be withdrawn, the Central Government shall serve a written notice on the governing body of the stock exchange.
- (ii) The said notice shall specify the reasons for the proposed withdrawal of the recognition.
- (iii) The governing body of the stock exchange shall be afforded an opportunity of being heard by the Central Government.
- (iv) Even after hearing the governing body, the Central Government is satisfied that the recognition granted to the stock exchange should be withdrawn; the Central Government may, by way of a notification in the Official Gazette, withdraw the recognition granted to the stock exchange.

The proviso to the said section 5 states that no such withdrawal shall affect the validity of any contract entered into or made prior to the date of notification withdrawing the recognition 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 for the due performance of any contracts outstanding on that date.

Question 18

The Executive Committee of a recognized stock exchange desires to transfer certain duties and functions of a clearing house to a recently set up clearing corporation, incorporated as a company under the companies Act, 1956, examining the provisions of The Securities Contract (Regulation) Act, 1956. State the purposes for which such transfer of duties and functions can be made to clearing corporation.

What is the procedure to be adopted for such transfer of duties and functions?

(November 2008)

Answer

A recognized stock exchange may, with the prior approval of the Securities Exchange Board of India, transfer the duties and functions of a clearing house to a clearing corporation, being a company incorporated under the Companies Act, 1956 for the purpose of:

- (a) The periodical settlement of contracts and differences there under
- (b) The delivery of, and payment for, securities;
- (c) Any other matter incidental to, or connected with, such transfer

PROCEDURE

Every clearing corporation shall for the purpose of transfer of the duties and functions of a clearing house to clearing corporation, make byelaws and submit the same to the SEBI for approval.

The SEBI may, on being satisfied that it is in the interest of the trade and also in the public interest to transfer the duties and functions of the clearing house to a clearing corporation, grant approval to the byelaws submitted to it under sub-section (2) of Section 8A of the Securities Contracts (Regulation) Act, 1956 and approve transfer of the duties and function of a clearing house to a clearing corporation.

The provision of Sections 4 to 12 of the said act shall as far as may be apply to a clearing corporation as they apply in relation to a recognized stock exchange.

Question 19

Mr. Bansal holds certain securities on 31st March, 2008, issued in his favour under the "Collective Investment Scheme." For a consideration, Mr. Bansal transferred the said securities in favour of another person. One month after the date on which the income on these securities became due, the transferee lodged the instrument of transfer. Decide in the light of the provisions of the Securities Contracts (Regulation) Act, 1956.

- (i) *Whether in the given case Mr. Bansal is entitled to receive and retain the income on these securities for the financial year ended 31st March, 2008?*
- (ii) *What would be your answer in case the transferee lodged the instrument of transfer 10 days after the date on which the income on these securities became due?*

(November 2008)

Answer

TRANSFER OF SECURITIES:

The problem as asked in the question is based on the provisions of Section 27A of the Securities contracts (Regulation) Act, 1956, wherein it shall be lawful for the holder of any securities, being units or the other instruments issued by collective investment scheme, whose

name appears on the books of the scheme, issuing the said security to receive and retain any income in respect of units issued by the scheme in respect thereof for any year, notwithstanding that the said security, being units issued by the scheme, has already been transferred by him for consideration, unless the transferee who claims the income in respect of units issued by the scheme from the transferor has lodged the security and all other documents relating to the transfer which may be required by the scheme with the scheme for being registered in his name within 15 days of the date on which the income in respect of units or other instruments issued under the scheme become due. The period of 15 day can be extended in certain contingencies as stated in explanation to Section 27A (1) of the said Act.

Thus,

- (i) the holder of the securities i.e Mr. Bansal, the transferor has right to receive or retain the income of the said securities for the financial year ended 31st March 2008, since the instrument for transfer was lodged one month after the date on which the income became due.
- (ii) the answer in the second case would differ. The holder i.e. Mr. Bansal, the transferor can not receive and retain the income since the instrument for transfer was lodged with the company within the statutory period of 15 days by the transferee. Accordingly the transferee would be entitled to receive the income on these securities.

Question 20

M/s Goyanka & Company, which is a member of a recognised stock exchange desire to buy and sell shares of Crossroads Company Limited on their own count as well as on behalf of investors. Advise M/s Goyanka & Company whether there are any restrictions for dealing in securities on their own count under the provisions of the Securities Contracts (Regulation) Act, 1956.

(May 2009)

Answer

SHARE TRANSACTIONS BY MEMBERS OF STOCK EXCHANGE AS PRINCIPALS:

Members of stock exchange normally carry out transactions on behalf of investors and hence principal and agent relationship exists between them. A member can enter into transaction as principal with another member of the exchange only. If a member of stock exchange desires to enter into contract as principal with a non member then he has to get written consent from such person to act as principal. The contract note should indicate that he is acting as principal. (Section 15 of the Securities Contracts (Regulation) Act, 1956).

Where the member has obtained the consent of such person otherwise than in writing he shall secure written confirmation by such person or such consent within three days from the date of such contract.

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However, such written consent of such person is not necessary for closing outstanding contract entered into by such person in accordance with the bye-laws, if the member discloses in the note, memorandum or agreement of sale or purchase in respect of such closing out that he is acting as principal.

Spot delivery contracts are not within the purview of section 15 of the said Act. (Section 18).

Thus M/s Goyanka & Company working as stock broker must bear in mind the above restrictions while entering into any transaction as principal with a non – member

Question 21

The Mewar Rural Financial Corporation, Udaipur, established under a special statute issued 5 years bonds to public directly and not through any Stock Exchange. Decide whether the said act of the Mewar Rural Financial Corporation is in violation of the provisions of the Securities Contracts (Regulation) Act, 1956.
(May 2009)

Answer

DIRECT ISSUE OF BONDS BY CORPORATION:

In order to prevent undesirable transactions in securities and to promote healthy stock market, the Securities Contracts (Regulation) Act, 1956 was enacted. Stock Exchanges are recognised under the Act. Section 73 of the Companies Act, 1956 lays down that offer of shares and debentures to public for subscription shall only be made after obtaining the permission of the stock exchange.

Section 28 of the Securities Contracts (Regulation) Act, 1956 lays down that the provisions of the Act shall not apply to the Government, Reserve Bank of India, any local authority or any corporation set up by a special law or any person who has effected any transaction with or through the agency of any such authority as stated above.

As given in the question, the Mewar Rural Financial Corporation is a corporation established under a special statute enacted by competent legislature. Therefore, the said corporation need not require to seek permission of any stock Exchange for the said purpose because it is exempted from the requirement given in the legislation.

There is no violation of the provisions of the Securities Contracts (Regulation) Act, 1956 because the provisions of Section 28 of the said act are not applicable to the said corporation.

Question 22

Industrial Finance Corporation of India, established under the Industrial Finance Corporation Act, 1948 having its registered office at Mumbai issued 8% Redeemable Bonds redeemable after 7 years. These bonds were issued directly to the members of the public and not through mechanism of Stock exchanges.

The Securities Contracts (Regulation) Act, 1956

You are required to state with reference to the provisions of Securities Contracts (Regulation) Act, 1956, whether such direct issue of bonds by the Industrial Finance Corporation of India is not violating the provisions of the said Act. (CA Final, New Course, (May 2009)

Answer

In order to prevent undesirable transactions in securities and to promote healthy stock market, the Securities Contracts (Regulation) Act, 1956 was enacted and all the Stock Exchanges in the country are registered under this Act. Section 73 of the Companies Act, 1956 states that offer of shares or debentures to public for subscription shall be made only after the permission of a Stock exchange.

Section 28(1) of the Securities Contracts (Regulation) Act, 1956 states that the provisions of this Act shall not apply to the Government, the Reserve Bank of India, any local authority, or corporation set up by a special law or any person who has effected any transaction with or through the agency of any such authority as stated earlier.

As stated in the question Industrial Finance Corporation of India is a corporation set up under the Industrial Finance Corporation Act, 1948. i.e. under a special statute enacted by the Parliament. Therefore, this Corporation does not need any permission from a Stock Exchange to issue any Bond or other securities. Accordingly, it has not violated the provisions of the Securities Contracts (Regulation) Act, 1956. The nature and tenure of the Bonds are immaterial.

Question 23

- (a) *A stock exchange desirous of taking over another stock exchange, seeks your advice on corporatisation. Examining the provisions of the Securities Contracts (Regulation) Act, 1956 and the meaning of the terms 'corporatisation' and 'demutualisation', advise the stock exchange about the steps to be taken to give effect to the scheme of corporatisation.*
- (b) *Mr. Veer a newly entered investor in the field of securities business seeks your advice on the investments to be made in securities of large Companies for long term purposes. With this object in view, he wants to know the meaning of the following terms commonly used in any stock exchange.*
- (i) *Derivative*
 - (ii) *Option in securities*
 - (iii) *Spot delivery contract.*

Advise suitably.

(November, 2009)

Answer

(a) CORPORATISATION & DEMUTUALISATION OF STOCK EXCHANGES

'Corporatisation' means the succession of a recognized stock exchange, being a body of individuals or a society registered under the Societies Registration Act, 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 'Demutualisation' means the segregation of ownership and management from the trading rights of the members of a recognized stock exchange in accordance with a scheme approved by the SEBI.

Steps for Corporatisation and Demutualization [Section 4B - Securities Contracts (Regulations) Act, 1956]

In accordance with the provisions of the Securities Contracts (Regulation) Act, 1956, as contained in Section 4B:

1. All recognized stock exchanges referred to in Section .4A shall, within such time as may be specified by the SEBI submit a scheme for corporatisation and demutualization for its approval.
2. On receipt of the scheme, the SEBI 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 shall be approved by the SEBI if the issue of shares for a lawful consideration or provision of trading rights in lieu of membership card of the members of a recognized 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, the scheme so approved shall be published immediately by-
 - (a) The SEBI in the Official Gazette
 - (b) The recognised Stock Exchange in such two daily newspapers circulating in India, as may be specified by the SEBI, 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 recognized stock exchange and on all persons having any contract, right, power, obligation or liability with, against, over, to, or in connection with, the recognized stock exchange or its members.
5. Where the SEBI is satisfied that it would not be in the interest of the trade and also in the public interest to approve the scheme, it may, by an order, reject the scheme and such order of rejection shall be published by it in the Official Gazette. SEBI shall give a reasonable opportunity of being heard to all the persons concerned and the recognized stock exchange concerned before passing an order rejecting the scheme.

6. SEBI may, while approving the scheme by an order in writing, restrict -
 - (a) the voting rights of the shareholders who are stock brokers of the recognized stock exchange.
 - (b) the right of shareholders or a stock broker of the recognized stock exchange to appoint the representatives on the governing board or the stock exchange.
7. The order made by SEBI shall be published in the Official Gazette and on the publication thereof, the order, notwithstanding anything to the contrary contained in the Companies Act, 1956, or any other law for the time being in force, have full effect.
8. Every recognized stock exchange, in respect of which the scheme for corporatisation or demutualization has been approved 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 SEBI, ensure that at least 51% of its equity share capital is held, within 12 months from the date of publication of the order by the public other than shareholders having trading rights. The SEBI may, on sufficient cause being shown to it and in the public interest, extend the said period by another 12 months.
 - (a) Mr. Veer, a new investor, desirous of entering investments business in any Stock Exchange, can be advised on different terms commonly used in any Stock Exchange.

(i) DERIVATIVE:

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 contract, which derives its value from the prices or index of prices, of underlying securities.

(ii) OPTION IN SECURITIES:

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 securities.

(iii) SPOT DELIVERY CONTRACT

Spot delivery contract means a contract which provides for:

- (i) 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 dispatch of the securities or the remittance of money therefore through the post

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being excluded from the computation of the period aforesaid if the parties to the contract do not reside in the same town or locality.

- (ii) 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.

Question 24

- (a) *MNC Limited whose shares are listed on a recognized Stock Exchange, are delisted by the Stock Exchange. The company seeks your advise on the remedies available to the company against the order of the Stock Exchange. Referring to the provisions of the Securities Contracts (Regulation) Act, 1956, advise the company.*
- (b) *Referring to the provisions of the Securities Contracts (Regulation) Act, 1956:*
 - (i) *Examine the extent to which the Central Government is empowered to suspend business of a recognized Stock Exchange.*
 - (ii) *The Central Government has granted recognition to a Stock Exchange. To what conditions may such a recognition be subject to?* **(May, 2010)**

Answer

- (a) Section 21A of the Securities Contracts (Regulation) Act, 1956 describes the provisions regarding delisting of securities by a recognised stock exchange.
 - (1) A recognized stock exchange may delist the securities, after recording the reasons therefore, from any recognized stock exchange on any of the ground or grounds as may be prescribed under this Act: Provided that the securities of a company shall not be delisted unless the company concerned has been given a reasonable opportunity of being heard.
 - (2) A listed company or an aggrieved investor may file an appeal before the Securities Appellate Tribunal against the decision of the recognized stock exchange delisting the securities within fifteen days from the date of the decision of the recognized stock exchange delisting the securities and the provisions of sections 22B to 22E of this Act shall apply, as far as may be, to such appeals; Provided that the Securities Appellate Tribunal may, if it is satisfied that the company was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding one month. MNC Ltd. may be advised accordingly.
- (b) (i) **Power of the Central Government to suspend business at a Stock Exchange: Section 12, Securities Contracts (Regulations) Act, 1956.**

If in the opinion of the Central Government an emergency has arisen and for the

purpose of meeting of the emergency the Central Government considers it expedient so to do, it may, by Notification in the Official Gazette, for reasons to be set out therein, direct a recognized stock exchange to suspend such of its business for such period not exceeding 7 days and subject to such conditions as may be specified in the notification, and if in the opinion of the Central Government the interest of the trade or the public interest requires that the period should be extended, may, by like notification extend the said period from time to time. Provided that where the period of suspension is to be extended beyond the first period, no notification extending the period of suspension shall be issued unless the Governing Body of the recognized Stock Exchange has been given an opportunity of being heard in the matter.

(ii) **Grant of recognition to stock exchanges - Conditions: Section 4(2), SCR, Act, 1956**

The conditions may include, condition relating to:

- (1) qualification for Membership of the Stock Exchange.
- (2) manner in which contracts shall be entered into and enforced as between members.
- (3) representation of the Central Government. on the Stock Exchange (not exceeding 3 nominated by the Central Government.)
- (4) maintenance of Accounts of members and their audit by Chartered Accountants wherever audit is required by the Central Government.