

[MODULE 2] Regulatory Framework Governing Stock Exchanges

as per Securities Contracts Regulation Act, 1956

Introduction to the Act

- In a corporate form of organisation heavy investment is made in "shares" of companies. Apart from that there are debentures. All these are called securities. These securities are tradable in market. The market for securities is called securities market or Capital Market.
- To prevent undesirable transactions in securities and to promote healthy stock market, the Securities Contract (Regulation) Act, 1956 (SCRA) was enacted by the parliament.
- SEBI is the authority to exercise control over capital market and enhance it's capital growth.

Definitions

Securities

"securities" - include

- 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;
- derivative;
- units or any other instrument issued by any collective investment scheme to the investors in such schemes;
- security receipt as defined in clause (2g) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
- units or any other such instrument issued to the investors under any mutual fund scheme.

Ready Delivery Contract

“ready delivery contract” means a contract which provides for the delivery of goods and the payment of a price therefor, either immediately, or within such period not exceeding eleven days after the date of the contract and subject to such conditions as the Central Government may, by notification in the Official Gazette.

Spot Delivery Contract

“spot delivery contract” means a contract which provides for,

- actual delivery of securities and the payment of a price therefor 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 therefor 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
- 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.

Stock Exchange

"stock exchange" means

- any body of individuals, whether incorporated or not, constituted before corporatisation and demutualisation under section 4A and 4B, or
 - a body corporate incorporated under the Companies Act, 1956 (1 of 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.

Corporatisation and Demutualisation of Stock Exchanges

- On and from the appointed date, all recognised stock exchanges 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.

Procedure

- All recognised stock exchanges referred to in section 4A shall 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.
- On receipt of the scheme referred to in sub-section 1, the SEBI may approve the scheme with or without modification.
- 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 assets of that stock exchange.
- Where the scheme is approved under sub-section (2), the scheme so approved shall be published immediately by-
 - the SEBI in the Official Gazette;
 - by the recognised Stock Exchange in such two daily newspaper circulating in India.
- 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.

Withdrawal

- 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 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.

- 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 stand withdrawn and the Central Government shall publish, by notification in the Official Gazette, such withdrawal of recognition.

Section 7A: Power of Recognised Stock Exchange to Make Rules Restricting Voting Rights, etc.

- A recognised stock exchange may make rules or amend any rules made by it to provide for all or any of the following matters, namely:
 - the restriction of voting rights
 - the regulation of voting rights
 - the restriction on the right of a member to appoint another person as his proxy
 - such incidental, consequential and supplementary matters as may be necessary to give effect to any of the matters specified in clauses (a), (b) and (c).
- No rules of a recognised stock exchange made or amended in relation to any matter referred to in clauses (a) to (d) of sub-section (1) shall have effect until they have been approved by the Central Government and published by that government in the Official Gazette.

Section 8: Power of Central Government to Direct Rules to be Made or to Make Rules

- Where, after consultation with the governing bodies of stock exchanges generally or with the governing body of any stock exchange in particular, the Central Government is of opinion that it is necessary to make any rules or to amend any rules already made in respect of all or any of the matters specified in sub-section (2) of section 3 within a period of two months from the date of the order.
- If any recognised stock exchange fails or neglects to comply with any order made under sub-section (1) within the period specified therein, the Central Government may make the rules for, or amend the rules made by, the recognised stock exchange.
- Where in pursuance of this section any rules have been made or amended, the rules so made or amended shall be published in the Gazette of India and also in the Official Gazette or Gazettes of the States or States in which the principal office or offices of the recognised stock exchange or exchanges is or are situate.

Section 10: Power of SEBI to Make or Amend Bye-Laws of Recognised Stock Exchanges

- The Securities and Exchange Board of India may, either on a request in writing received by it in this behalf from the governing body of a recognised stock exchange or on its own motion, make bye-laws for all or any of the matters specified in Section 9 or amend any bye-laws made by such stock exchange under that section.
- Where in pursuance of this section any bye-laws have been made or amended the bye-laws so made or amended shall be published in the Gazette of India and also in the Official Gazette of the State in which the principal office of the recognised stock exchange is situate, and on the publication thereof in the Gazette of India, the bye-laws so made or amended shall have effect as if they had been made or amended by the recognised stock exchange concerned.

- Notwithstanding anything contained in this section, where the governing body of a recognised stock exchange objects to any bye-laws made or amended under this section by the SEBI on its own motion, it may, within two months of the publication apply to the SEBI for revision thereof, and the SEBI may, after giving an opportunity to the stock exchange to be heard in the matter, revise the bye-laws so made or amended.
- The making or the amendment or revision of any bye-laws under this section shall in all cases be subject to the condition of previous publication.

Provided that if the Securities and Exchange Board of India is satisfied in any case that in the interest of the trade or in the public interest any bye-laws should be made, amended or revised immediately, it may, by order in writing specifying the reasons therefor, dispense with the condition of previous publication.

Books of Accounts to be maintained by Recognised Stock Exchange

Following Books of Accounts are to be maintained by Stock Broker (Regulation 17):

Every stock broker shall keep and maintain the following books of account, records and documents namely:

- Register of transactions (Sauda Book);
- Clients ledger;
- General ledger;
- Journals;
- Cash book;
- Bank pass book;
- Documents register containing inter alia, particulars of securities received and delivered in physical form;
- Members' contract books showing details of all contracts entered into by him with other members of the same exchange of counterfoils;
- Written consent of clients in respect of contracts entered into as principals;
- Margin deposit book;
- Registers of accounts of sub-brokers;
- An agreement with a sub-broker specifying the scope of authority and responsibilities of the Stock-Broker and such sub-broker;
- Client Account Opening form in the format as may be specified by the Board.

Maintenance of Books of Account and Records

Every stock broker shall preserve the books of account and other records maintained under regulation 17 for a minimum period of five years. Further, in case such documents are maintained in electronic form, provisions of Information Technology Act, 2000 in this regard shall be complied with.

Grounds on which Stock Exchange can delist the securities of a company (Section 3 to 20)

Application for Recognition of Stock Exchanges (Section 3)

- 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.
- Every application 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 :
 - the governing body of such stock exchange
 - the powers and duties of the office bearers of the stock exchange,
 - the admission into the stock exchange of various classes of members, the qualifications for membership, and the exclusion, suspension, expulsion and readmission of members therefrom or therein to,
 - the procedure for the registration of partnerships as members of the stock exchange.

Grant of Recognition to Stock Exchanges (Section 4)

If the Central Government is satisfied, after making such inquiry as may be necessary in this behalf and after obtaining such further information, if any, as it may require:

- 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.
- 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.
- 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 as of the stock exchange is situated.

Power of Central Government to Call for Periodical Returns or Direct Inquiries to be made (Section 6)

- Every recognised stock exchange shall furnish to the Securities and Exchange Board of India such periodical returns relating to its affairs as may be prescribed,
- Every recognised stock exchange and every member thereof shall maintain and preserve for such periods not exceeding five years
- Where an inquiry in relation to the affairs of a recognised stock exchange or the affairs of any of its members in relation to the stock exchange has been undertaken under:
 - every director, manager, secretary or other officer of such stock exchange,
 - every member of such stock exchange,
 - if the member of the stock exchange is a firm, every partner, manager,
 - secretary or other officer of the firm

Annual Reports to be Furnished to Central Government by Stock Exchanges (Section 7)

Every recognised stock exchange shall furnish the Central Government with a copy of the annual report, and such annual report shall contain such particulars as may be prescribed.

Power of Recognised Stock Exchanges to make Bye-laws (Section 9)

- Any recognised stock exchange may, subject to the previous approval of the SEBI, make bye-laws for the regulation and control of contracts.
- In particular, and without prejudice to the generality of the foregoing power, such bye-laws may provide for:
 - the opening and closing of markets and the regulation of the hours of trade
 - a clearing house for the periodical settlement of contracts and differences thereunder, the delivery of and payment for securities, the passing on of delivery orders and the regulation and maintenance of such clearing house
 - the submission to the Securities and Exchange Board of India by the clearing house as soon as may be after each periodical settlement of all
- The publication by the clearing house of all or any of the particulars submitted to the SEBI subject to the directions if any, issued by the SEBI in this behalf,
 - the number of classes of contracts in respect of which settlements shall be made or differences paid through the clearing house,
 - the regulation, or prohibition of budlas or carry-over facilities,
 - the fixing, altering or postponing of days for settlements,
 - the method and procedure for the settlement of claims or disputes,
 - the levy and recovery of fees, fines and penalties,
 - the regulation of dealings by members for their own account,
 - the separation of the functions of job seekers and brokers,
 - the limitations on the volume of trade done by any individual member in exceptional circumstances.

Power to Suspend Business of Recognised Stock Exchanges (Section 12)

If in the opinion of the Central Government an emergency has arisen and for the purpose of meeting the emergency the Central Government considers it expedient so to do, it may, by notification in the Official Gazette, direct a recognised stock exchange to suspend such of its business for such period not exceeding seven days, 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.

Contracts in Notified Areas Illegal in Certain Circumstances (Section 13)

If the Central Government is satisfied, having regard to the nature or the volume of transactions in securities in any State or States or area that it is necessary so to do it may, by notification in the Official Gazette, declare this section to apply to such 43 State or States or area, and there upon every contract which is entered into after the date of the notification.

Contracts in Notified Areas to be Void in Certain Circumstances (Section 14)

Any contract entered into in any State or area specified in the notification under section 13 which is in contravention of any of the bye-laws specified in that behalf shall be void:

- as respects the rights of any member of the recognised stock exchange who has entered into such contract in contravention of any such bye-law, and also
- as respects the rights of any other person who has knowingly participated in the transaction entailing such contravention.

Members May Not Act as Principals in Certain Circumstances (Section 15)

No member of a recognised stock exchange shall in respect of any securities enter into any contract as a principal with any person other than a member of a recognised stock exchange, unless he has secured the consent or authority of such person and "between members of a recognised stock exchange" discloses in the note, memorandum or agreement of sale or purchase that he is acting as a principal provided that where the member has secured the consent or authority of such person.

Power to Prohibit Contracts in Certain Cases (Section 16)

- If the Central Government is of opinion that it is necessary to prevent undesirable speculation in specified securities in any State or area, it may, by notification in the Official Gazette, declare that no person in the State or area specified in the notification, shall, save with the permission of the Central Government, enter into any contract for the sale or purchase of any security.
- All contracts in contravention of the provisions entered into after the date of notification issued thereunder shall be illegal.

Licensing of Dealers in Securities in Certain Areas (Section 17)

- No person shall carry on or purport to carry on, whether on his own behalf or on behalf of any other person, the business of dealing in securities in any State or area to which section 13 has not been declared to apply and to which the Central Government may, by notification in the Official Gazette, declare this section to apply.
- No notification shall be issued with respect to any State or area unless the Central Government is satisfied, having regard to the manner in which securities are being dealt with in such State or area.

Exclusion of Spot Delivery Contracts (Section 18)

- Nothing contained in sections 13, 14, 15 and 17 shall apply to spot delivery contracts.
- If the Central Government is of opinion that in the interest of the trade or in the public interest it is expedient to regulate and control the business of dealing in, spot delivery contracts also in any State or area has been declared to apply to that State or area or not, it may, by notification in the Official Gazette, declare that the provisions of section 17 shall also apply to such State or area in respect of spot delivery contracts.

Stock Exchanges other than Recognised Stock Exchanges Prohibited (Section 19)

- No person shall, except with the permission of the Central Government, organise or assist in organising or be a member of any stock exchange other than a recognised stock exchange for the purpose of assisting in, entering into or performing any contracts in securities.
- This section shall come into force in any State or area on such date as the Central Government may, by notification in the Official Gazette, appoint.

Prohibition of Options in Securities (Section 20)

Prohibition of options in securities:

- All options in securities entered into after the commencement of this act shall be illegal.
- Any option in securities which has been entered into before such commence and which remains to be performed, whether wholly or in part, after such commencement shall, to this extend, become void.
