

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA

EXIT ORDER IN RESPECT OF:

UTTAR PRADESH STOCK EXCHANGE LIMITED

1. U.P. Stock Exchange Limited (hereinafter referred to as the “UPSE” and formerly known as “the U.P. Stock Exchange Association Ltd.”, Kanpur) was incorporated as a company limited by shares under the Companies Act, 1956 on November 15, 1979. The Central Government had granted recognition to UPSE, as a stock exchange under the provisions of section 4 of the Securities Contracts (Regulation) Act, 1956 (hereinafter referred to as the “SCRA”) on June 03, 1982 and renewed from time to time under rule 7 of the Securities Contracts (Regulation) Rules, 1957 (hereinafter referred to as the “SCRR”).
2. The recognition of UPSE was last renewed by Securities and Exchange Board of India (hereinafter referred to as “SEBI”) for a period of one year commencing on June 3, 2013 and ending on June 2, 2014. The renewal was, however, subject to the condition that *“the Exchange can commence trading in securities only after complying with all the regulatory requirements imposed by the Securities and Exchange Board of India and the Exchange shall comply with such other conditions prescribed by SEBI from time to time”*.
3. SEBI, vide Circular No. MRD/DoP/SE/Cir-36/2008 dated December 29, 2008, issued Guidelines and laid down the framework for exit by stock exchanges whose recognition is withdrawn and/or renewal of recognition is refused by SEBI and who may want to surrender their recognition. The said Guidelines were reviewed and modified vide Circular No. CIR/MRD/DSA/14/2012 dated May 30, 2012 (hereinafter referred to as "Exit Circular, 2012"). In terms of clause 2.2 of the Exit Circular, 2012, a stock exchange, where the annual trading turnover on its platform is less than ₹1,000 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 the said Circular. In terms of clause 2.3 of the said Circular, if any stock exchange failed to achieve a turnover of ₹1,000 crore, it would be subject to compulsory exit process.
4. The shareholders of UPSE in its Extra Ordinary General Meeting held on June 30, 2014 passed the resolution for exiting as a stock exchange through voluntary surrender of recognition. In this regard, vide letter dated July 01, 2014, UPSE made a request to SEBI for its exit as stock exchange informing thereby that the shareholders of UPSE, at the Extra Ordinary General Meeting held on June 30, 2014, approved the resolution for exit through voluntary surrender of

recognition as per the Exit Circular, 2012.

5. Accordingly, I proceed to deal with the exit request of UPSE in terms of clause 2.2 of the Exit Circular, 2012. I note that as per the Exit Circular, 2012, *inter alia*, the following conditions are required to be complied by the de-recognised/non-operational stock exchanges for seeking exit:
- (a). Permission to distribute its assets subject to certain conditions as laid down in the circular as well as the other guidelines that may be issued by SEBI, Governments or any other statutory body from time to time.
 - (b). For the purpose of valuation of the assets of the stock exchange, a valuation agency appointed by SEBI shall submit its report.
 - (c). The quantum of assets for distribution will be available after payment of the following by the stock exchange:
 - (i) Statutory dues including Income Tax;
 - (ii) Transfer of Investor Protection Fund, Investor Services Fund, 1% security deposit available with the Exchange to SEBI Investor Protection and Education Fund (hereinafter referred to as the "IPEF");
 - (iii) The exiting exchange shall pay the following dues to SEBI:-
 - Dues outstanding to SEBI including 10% of the listing fee and the annual regulatory fee;
 - The outstanding registration fees of brokers/trading members of such de-recognised stock exchanges as specified in the Securities and Exchange Board of India (Stock Brokers and Sub Brokers) Regulations, 1992, till the date of such de-recognition;
 - In case of any shortfall in collection of dues of the brokers to SEBI, the exiting Stock Exchange will make good the shortfall;
 - (iv) Refund of deposit (refundable) to the stock brokers including their initial contribution/deposit to Settlement Guarantee Fund/Trade Guarantee Fund (SGF/TGF).
 - (d). Contribution of up to 20% of its assets (after tax) towards IPEF taking into account, *inter alia*, the governance standards of the stock exchange and estimation of future liabilities.
 - (e). The companies exclusively listed on the stock exchange seeking exit shall list their securities on any other recognised stock exchange. If such exclusively listed companies fail to obtain listing on any other recognised stock exchange, they will cease to be listed companies and will be moved to the dissemination board by the exiting stock exchange. Such dissemination

board would be provided by a Stock Exchange with nationwide trading terminals. The exiting stock exchange as well as exchange providing dissemination board will give wide publicity about the dissemination board in one leading national daily and one local daily.

- (f). The exiting stock exchange shall set aside sufficient funds in order to provide for settlement of any claims, pertaining to pending arbitration cases, arbitration awards, not implemented, if any, liabilities/claims of contingent nature, if any, and unresolved investor complaints/grievances lying with it.
 - (g). The exiting exchange may provide trading opportunity to their trading members to trade on stock exchanges having nationwide terminals through their subsidiary company, which will function as a normal broking entity.
6. I have considered all relevant documents available on record for the purpose of considering the case of exit of UPSE. With regard to the income tax obligation in respect of transfer of capital assets of a stock exchange, I note that section 47(xiii) of the Income Tax Act, 1961 provides as under:-

Section 47 (xiii):

Nothing in Section 45 applies to any transfer of a capital asset or intangible asset by a firm to a company as a result of succession of the firm by a company in the business carried on by the firm, or any transfer of a capital asset to a company in the course of demutualisation or corporatisation of a recognised stock exchange in India as a result of which an association of persons or body of individuals is succeeded by such company:

Provided that –

(e) the demutualisation or corporatisation of a recognised stock exchange in India is carried out in accordance with a scheme for demutualisation or corporatisation which is approved by the Securities and Exchange Board of India established under section 3 of the Securities and Exchange Board of India Act, 1992 (15 of 1992);]”

7. In respect of the tax treatment to a stock exchange post its corporatisation and demutualization, the following recommendation of the Justice Kania Committee which was the basis for the amendment in section 47(xiii) of the Income Tax Act, 1961 to provide tax benefit to the corporatized and demutualised stock exchanges is worth mentioning:

“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”.

8. The corporatisation and demutualisation scheme of UPSE was approved by SEBI vide notification no. SEBI/MRD/48113/2005 dated August 29, 2005 (hereinafter referred as "the scheme"). The scheme, *inter alia*, provided for the segregation of ownership and management from the trading rights of the members, restriction on voting rights of shareholders who are also trading members, composition of the Governing Board, etc. in accordance with the provisions of section 4B (6) of the SCRA, 1956 utilization of assets and reserves and other matters required for the purpose of and in connection with the corporatisation and demutualisation of UPSE.
9. In terms of condition mentioned in para 5(b) above, SEBI, in consultation with UPSE, appointed M/s. Prasad Gupta J. & Co. as the Valuation Agency on September 16, 2014 for verification and valuation of assets and liabilities of UPSE. The Valuation Agency submitted its report vide letter dated December 23, 2014.
10. With respect to the compliance of conditions specified in the Exit Circular, 2012 by UPSE and settlement of its liabilities observed by the Valuation Agency, I note that:
 - (a). In compliance with condition mentioned in para 5(c)(ii) above, as advised by SEBI, UPSE has transferred to SEBI - Investor Protection and Education Fund (IPEF)
 - an amount of ₹8,17,26,743/- available in its 'Investor Protection Fund' through Real Time Gross Settlement (RTGS) on February 26, 2015; and
 - an amount of ₹1,65,83,179/- available in its 'Investor Services Fund' through Cheque no. "502509" dated January 16, 2015.
 - (b). As per the valuation report, '1% security deposit' outstanding as on September 30, 2014 is ₹31,750/-. It is noted that the valuation agency had calculated this amount on refundable deposits of stock brokers instead of 1% security deposit of the companies. Vide its letter dated January 16, 2015, UPSE has stated that the actual amount available is Nil. UPSE has further stated that on non-compliance of the Listing Agreement by the listed companies as per the observation of the SEBI Inspection Report, 2008, it had forfeited the amount that was lying as 1% security deposit in the year 2010-11 and treated the same as income in the financial year 2010-11.
 - (c). In compliance with condition mentioned in para 5(c) (iii) above, UPSE has paid necessary dues outstanding to SEBI including 10% of the listing fee and the annual regulatory fee. UPSE, through RTGS dated March 27, 2015, has also paid the outstanding registration fees

amounting to ₹96,16,931/- of brokers dues as specified in the Securities and Exchange Board of India (Stock Brokers and Sub Brokers) Regulations, 1992 till the date of such de-recognition.

- (d). In compliance with condition mentioned in para 5(c) (iv) above, UPSE has given an undertaking dated March 24, 2015 that it will not distribute any assets before clearing the liabilities in that regard.
 - (e). In compliance with condition mentioned in para 5(d) above, UPSE has contributed an amount to ₹20,00,000/- through RTGS dated March 27, 2015 towards IPEF.
 - (f). In compliance with condition mentioned in para 5(e) above, UPSE has stated in its undertaking that it has taken necessary steps in terms of the Exit Circular, 2012 and SEBI circular dated May 22, 2014 and other circular/directions issued by SEBI from time to time. It has further undertaken to extend all the co-operation to SEBI and other regulatory authorities with regards to any matters/issues that may arise subsequently.
 - (g). In compliance with condition mentioned in para 5(f) above, UPSE has submitted an undertaking dated March 24, 2015 stating that there are no arbitration disputes/investor complaints pending and that it will clear all the liabilities before distribution of assets of UPSE.
 - (h). With regard to its other liabilities and contingent liabilities as pointed out by the Valuation Agency, UPSE vide an undertaking dated March 24, 2015 has undertaken to clear the said liabilities before the distribution of its assets and to clear any additional amount that may become liable to be paid on account of any of the stated liabilities in the said undertaking.
 - (i). In compliance of condition mentioned in para 5(g) above, Vide undertaking dated March 24, 2015 UPSE has undertaken and declared that UPSE Securities Limited, a functional subsidiary of UPSE is a corporate member of BSE, NSE, MCX and depository services (depository participant of CDSL) and is providing trading facilities to all UPSE Members.
 - (j). UPSE has also given an undertaking dated March 24, 2015 stating that the details of cases as submitted to SEBI lodged against it are the only cases pending before various legal fora and it has undertaken to assume complete responsibility for the financial implication of any claims against it that may arise at any future date as an outcome of the resolution/settlement of those cases.
11. From the valuation report and undertaking dated March 24, 2015 of UPSE, it is observed that all the known liabilities have been brought out and that there is no future liability that is not known

as on date. I note that UPSE has substantially complied with the conditions contained in the Exit Circular, 2012 subject to its undertakings. I, therefore, am of the view that it is a fit case to allow exit to UPSE in terms of clause 8 of the Exit Circular, 2012.

12. I, therefore, in exercise of the powers conferred upon me by virtue of section 19 read with provisions of section 11(1), section 11(2) (j) of the Securities and Exchange Board of India Act, 1992 and sections 4, 5 and 12A of the SCRA, allow the exit of Uttar Pradesh Stock Exchange Limited as a stock exchange and hereby direct UPSE to:-

- (a). Comply with its tax obligations under Income Tax Act, 1961;
- (b). Comply with the undertakings given by it to SEBI;
- (c). Comply with other consequential conditions of Exit Circular, 2012; and
- (d). Change its name and not to use the expression "Stock Exchange" or any variant of this expression in its name and to avoid any representation of present or past affiliation with the stock exchange, in all media.

13. This order shall come into force with immediate effect. A copy of this order shall be forwarded to the Income Tax Authorities, the State Government of Uttar Pradesh and the Ministry of Corporate Affairs intimating the exit of Uttar Pradesh Stock Exchange Limited and for appropriate action at their end as per applicable laws.

Sd/-

DATE: JUNE 9th, 2015

PLACE: MUMBAI

RAJEEV KUMAR AGARWAL

WHOLE TIME MEMBER

SECURITIES AND EXCHANGE BOARD OF INDIA