

**BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA****ORDER**

**UNDER SECTIONS 11 AND 11B OF SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 AND SECTION 12A OF SECURITIES CONTRACTS (REGULATION) ACT, 1956, READ WITH REGULATION 49 OF THE SECURITIES CONTRACTS (REGULATION) (STOCK EXCHANGES AND CLEARING CORPORATIONS) REGULATIONS, 2012.**

**In respect of Financial Technologies (India) Limited (FTIL)**

**Appearances:****For FTIL:**

1. Mr. Somasekhar Sundaresan, Advocate
2. Mr. KRCV Sesachalam, Advocate
3. Mr. Paras Parekh, Advocate
4. Mr. Ashish Kakade, Senior Manager, FTIL

**For SEBI:**

1. Mr. SVMD Rao, Executive Director
2. Mr. P K Bindlish, Chief General Manager
3. Mr. Sunil Kadam, General Manager
4. Mr. Santosh Shukla, Joint Legal Adviser
5. Ms. Vishakha More, Assistant General Manager
6. Mr. Parag K Sinha, Assistant Legal Adviser

1. The shareholding of Financial Technologies (India) Ltd. (hereinafter referred to as "FTIL") in several recognized stock exchanges and clearing corporation is as under:

<b>Sl. No.</b>	<b>Name of stock exchange/ clearing corporation</b>	<b>Number of shares/ warrants held</b>
1.	MCX Stock Exchange Limited (MCX-SX)	2,71,65,000 shares and 56,24,60,000 transferable warrants
2.	MCX Stock Exchange Clearing Corporation Limited (MCX-SX CCL):	57,50,000 shares.
3.	Delhi Stock Exchange Limited (DSE)	14,96,500 shares.
4.	Vadodara Stock Exchange Limited (VSE)	2,90,000 shares.
5.	National Stock Exchange of India Limited (NSEIL):	10000 shares

2. It was noted that the Forward Markets Commission (FMC) passed an order on December 17, 2013 against FTIL holding *inter alia* as under:

*“in the public interest and in the interest of the Commodities Derivatives Market which is regulated under FCRA, 1952, the Commission holds that Financial Technologies (India) Ltd (FTIL) is not a ‘fit and proper person’ to continue to be a shareholder of 2% or more of the paid-up equity capital of Multi Commodity Exchange of India Ltd. (MCX) as prescribed under the guidelines issued by the Government of India for capital structure of commodity exchanges post 5-years of operation. It is further ordered that neither FTIL, nor any company/entity controlled by it, either directly or indirectly, shall hold any shares in any association / Exchange recognised by the Government or registered by the FMC in excess of the threshold limit of the total paid-up equity capital of such Association / Exchange as prescribed under the commodity exchange guidelines and post 5-year guidelines”.*

3. In view of the above, it was noted that FTIL does not satisfy the fit and proper criteria as specified under regulation 20(1)(b)(v) read with regulation 19 of the Securities Contracts (Regulation)(Stock Exchanges and Clearing Corporations) Regulations, 2012 (the SECC Regulations) so as to hold shares in the abovementioned recognised stock exchanges and clearing corporations. In observance of principles of natural justice a notice dated December 20, 2013 and addendum thereto dated December 20, 2013 was issued to FTIL seeking its explanation in the matter.
4. Vide letters dated December 21, 2013, December 26, 2013 and February 10, 2014 FTIL filed its replies. FTIL was also granted opportunity of personal hearing on January 07, 2014, January 13, 2014, February 11, 2014 and March 06, 2014 when its authorised representatives had appeared and made submissions on behalf of FTIL. The oral submissions of FTIL on merits of the case were made on March 06, 2014 when Mr. Somasekhar Sundaresan, Advocate of FTIL made detailed submissions in defence of FTIL and also requested to defer the order or defer the implementation of the order that may be passed in the matter. He also requested time up to March 18, 2014 to file written submission in the matter which was filed vide letter dated March 18, 2014 of FTIL. The replies and submissions of FTIL are *inter alia* as following:
  - a) The notice proceeds on the fundamental premise of the order dated December 17, 2013 whereby FMC has declared FTIL as not fit and proper person to hold 2% or more of the equity share capital in the Multi Commodity Exchange of India Limited (MCX). The said order is under challenge before the Hon'ble Bombay High Court. Since the entire basis of the notice is under challenge and the Hon'ble Bombay High Court is

seized of the same, there is no urgency for SEBI to pre-empt the matter and pass any order on the notice.

- b) In para 21 of its affidavit filed before the Hon'ble Bombay High Court, FMC has admitted that it has not directed FTIL to divest its shareholding in MCX. That call has to be taken by MCX. Therefore, SEBI has to form an independent view without getting influenced by the FMC order.
- c) The Hon'ble Bombay High Court has admitted the writ petitions and will determine whether the FMC order is sustainable. Therefore, SEBI may not consider it appropriate to adjudicate the conflicting versions of FTIL and FMC that is the subject matter of the role that would be played by the Hon'ble Bombay High Court.
- d) Regulation 20 of the SECC Regulations provides the specific criteria for a person to be 'fit and proper' in terms of the SECC Regulations. Regulation 19 of the SECC Regulations merely stipulates that the requirement of being 'fit and proper' are to be met for holding any equity shares in a stock exchange or clearing corporation. Therefore, unless the criteria prescribed under regulation 20 are met, regulation 19 cannot be invoked. Regulation 20 of the SECC Regulations provides a deeming fiction to hold a person 'fit and proper' if such person has not incurred any of the disqualifications stipulated in clause (b) of sub-regulation (1) of regulation 20. A plain reading of regulation 20 (1)(b)(v) which is relevant in this case, shows that in order to incur the disqualification the order of any other regulatory authority against the person concerned ought to have a bearing on the securities market. Therefore, it is incumbent upon the notice to allege and demonstrate that FMC order against FTIL has in fact a bearing on the securities market. The burden of proof in this regard lies on SEBI.
- e) The notice merely proceeds on the basis that the passing of the FMC order operates as an automatic disqualification under regulation 20(1)(b)(v) of the SECC Regulations. It is vague and devoid in material particular that it does not give indication of any nature whatsoever as to how the FMC order causes any adverse bearing on the securities market by reason of the shareholding of FTIL in the relevant entities. Even the addendum dated March 03, 2014 does not contain any specific allegation in this regard. It is therefore apparent that there are no factors that SEBI can rely upon for alleging that passing of the FMC order has any bearing on the securities market. At the last personal hearing on March 6, 2014 it was suggested to FTIL that the bearing on the securities market was "obvious" and therefore, the notice need not actually set out what the apprehended bearing on the securities market would be. Such approach is alien to law and wholly untenable in as much as it requires FTIL to imagine and decipher the mind of the authority issuing the notice and also meet the charge. The alleged bearing

of the FMC order on the securities market is a material factor and without any allusion to why and how the FMC order has bearing on the securities market by reason of FTIL's holding in the relevant entities, the notice cannot be legitimate.

- f) The correct course of action for SEBI to undertake would be to issue a specific supplemental notice to put FTIL to terms as to the specific bearing on the securities market that SEBI is concerned about.
- g) Without prejudice to the submission that the notice is vitiated on account of non-furnishing of material particulars it is submitted that there are no foreseeable reasons on account of which any directions may be warranted against FTIL pursuant to the notice or otherwise. It is submitted that the shareholding of FTIL in the recognised stock exchanges and clearing corporation is insignificant and does not have any bearing on the securities market.
- h) MCX- SX has initiated a process of rights issue expanding its capital to thrice its size. FTIL will not participate in the rights issue. Therefore, FTIL's shareholding will automatically stand reduced to approximately 1.72% equity shares in MCX-SX assuming all other shareholders subscribe to the rights issue.
- i) The FMC order was not on the facts relating to MCX-SX. It was regarding 26% shareholding of FTIL in MCX.
- j) MCX-SX board of directors does not have a single nominee of FTIL.
- k) FTIL also holds 56,24,60,000 warrants in MCX-SX, none of which it is entitled to exercise for conversion into equity shares as per undertaking furnished by FTIL in this regard. Such warrants would entitle it to 19.52% in MCX-SX equity shares (post rights issue). In any case, FTIL is not desirous to convert the warrants or increase its voting rights in MCX-SX. FTIL has also proposed to undertake restraint on its voting rights till disposal of the case by the Hon'ble Bombay High Court.
- l) SEBI is aware that both the DSE and VSE are defunct and in fact, are completely inactive with no trading taking place. It is possible that these exchanges would in fact seek to shed their recognition as stock exchanges using the exit opportunity provided by SEBI. FTIL does not have any representation on both their boards of directors. Therefore, the question of "bearing on the securities market" does not arise in these cases.
- m) MCX-SX and NSEIL are, in fact, competitors. It is also a fact that FTIL and NSEIL fought legal battles on certain imaginary issues of software. Any shareholding in NSEIL's equity share capital in the hands of FTIL, regardless of whether the holding is miniscule, can never lead to FTIL having any say in the functioning and operation of NSEIL. Consequently, it goes without saying that FTIL's holding in NSEIL is wholly

irrelevant for the securities market, and therefore, there is no reasonable or rational basis to pass any order in connection with the same.

- n) It is apparent that FTIL's stakes in the recognized stock exchanges and clearing corporation is confined only to a limited economic interest in the same and does not entitle it to any management or control over these entities. Therefore, FTIL's shareholding in the recognized stock exchanges and clearing corporation has no bearing on the securities market.
5. I have carefully considered the notice, addendum thereto, the replies and submissions of FTIL, and relevant material available on record. I note that instant proceedings are pursuant to the FMC order dated December 17, 2013 holding FTIL not 'fit and proper person' to continue to hold 2% or 'more of the paid up equity capital of MCX. FTIL has contended that the FMC order has been challenged by it before the Hon'ble Bombay High Court and SEBI may not consider appropriate to adjudicate the versions of FTIL and FMC that is subject matter of the role that is to be played by the Hon'ble Bombay High Court. I note that the Hon'ble Bombay High Court has not stayed the effect and operation of the FMC order dated December 17, 2013 which has been challenged in the writ petition filed by FTIL. In fact, vide its order dated February 28, 2014 the Hon'ble Bombay High Court has refused the prayer of FTIL to grant such stay and has observed as following-

*"After having perused the impugned order, we find that elaborate enquiry has been made by the Commission. Findings of fact of serious nature have been recorded against the Petitioners. The fraud perpetrated is to the tune of Rs. 5,500 Crores. Criminal investigations are in progress. Considering the gravity of the allegations which have been found to be established against the Petitioners this is not a fit case where prayer for stay can be granted in exercise of writ jurisdiction under Article 226 of the Constitution of India. Accordingly prayer for interim relief is rejected. Hearing of the Petition is expedited."*

6. FTIL has also contended, in its reply dated February 10, 2014, that in its affidavit filed before the Hon'ble Bombay High Court, FMC has admitted that it has not directed FTIL to divest its shareholding in MCX. Therefore, in absence of any such direction by FMC, the notice which purports to direct FTIL to divest its stake in MCX-SX need not be acted upon while the Hon'ble Bombay High Court is seized of the matter. In this regard, I note that in the affidavit as claimed by FTIL, FMC has stated that it held that FTIL is not a 'fit and proper person' to continue to hold 2% or more of the paid up equity capital of MCX. In my view, the facts and laws challenged in the writ petition are not subject matter of the instant proceedings. In the instant proceedings the limited question is whether in view of the FMC

order dated December 17, 2013 FTIL attracts the disqualification stipulated in regulation 20(1)(b)(v) of the SECC Regulations. I, therefore, do not find any conflict with the said submissions of FMC as claimed by FTIL with the issues involved in the notice.

7. Considering the facts and circumstances of this case and in absence of any embargo imposed by law or the decision of the Hon'ble Bombay High Court, I deem it appropriate to proceed to decide the instant matter. In this case, on the basis of above mentioned observations of the FMC, FTIL is said to be disqualified under regulation 20(1)(b)(v) read with regulation 7(2) and 19(1) of the SECC Regulations to hold any share/warrants in the recognized stock exchanges and clearing corporations. The provisions of these regulations are reproduced as under:-

**Regulation 7 (2) (c ) of the SECC Regulations**

*"An applicant seeking recognition as a stock exchange or clearing corporation shall comply with the following conditions, namely:—*

*(a) .....*

*(b) .....*

*(c) the applicant, its directors and its shareholders who hold or intend to hold shares, are fit and proper persons as described in regulation 20;*

*....."*

**Regulation 19 (1) of the SECC Regulations**

*"No person shall, directly or indirectly, acquire or hold equity shares of a recognised stock exchange or recognised clearing corporation unless he is a fit and proper person."*

**Regulation 20 (1) of the SECC Regulations**

*"20. (1) For the purposes of these regulations, a person shall be deemed to be a fit and proper person if—*

*(a) such person has a general reputation and record of fairness and integrity, including but not limited to—*

*(i) financial integrity;*

*(ii) good reputation and character; and*

*(iii) honesty;*

*(b) such person has not incurred any of the following disqualifications—*

*(i) the person, or any of its whole time directors or managing partners, has been convicted by a court for any offence involving moral turpitude or any economic offence or any offence against the securities laws;*

*(ii) an order for winding up has been passed against the person;*

*(iii) the person, or any of its whole time directors or managing partners, has been declared insolvent and has not been discharged;*

*(iv) an order, restraining, prohibiting or debarring the person, or any of its whole time directors or managing partners, from dealing in securities or from accessing the securities market,*

- has been passed by the Board or any other regulatory authority, and a period of three years from the date of the expiry of the period specified in the order has not elapsed;*
- (v) *any other order against the person, or any of its whole time directors or managing partners, which has a bearing on the securities market, has been passed by the Board or any other regulatory authority, and a period of three years from the date of the order has not elapsed;*
- (vi) *the person has been found to be of unsound mind by a court of competent jurisdiction and the finding is in force; and*
- (vii) *the person is financially not sound."*

8. I find that the above scheme of the SECC Regulations with regard to determining whether a person is 'fit and proper person' to hold shares in a recognized stock exchange or clearing corporation is very clear. The provisions of the SECC Regulations in this regard are not linked to the quantum of shareholding of the concerned person, rather, it relates to his / her status. That status has to be determined in view of the criteria prescribed in regulation 20 of the Regulations. The criteria under regulation 20 of the SECC Regulations is both positive and negative. While clause (a) of regulation 20(1) of the SECC Regulations deals with positive attributes i.e. qualifications, clause (b) deals with negative attributes i.e. disqualifications. From the language of regulation 20, it is very clear that in order to acquire or hold any share in a recognized stock exchange or clearing corporation a person must satisfy both the requirements. If the person fails to satisfy either of the attributes, he cannot hold any share in a recognized stock exchange or clearing corporation. For the purposes of the SECC Regulations, as explained by regulation 16, these qualifications and disqualifications also extend with respect to holding of any instrument that provide for entitlement of equity or rights over equity at any future date.
9. I note that regulation 19(1) of the SECC Regulations is a negatively worded provision and has to be interpreted accordingly. The language of regulation 19(1) of the SECC Regulations which start with expression "*No person shall, directly or indirectly, acquire or hold .....*" clearly indicates that its provisions are mandatory. These provisions have clothed their command in negative form which insists on their compliance as they are enacted. In this regard, the following observations of Hon'ble Supreme Court in the matter of *Mannalal Khetan and Ors. Vs. Kedar Nath Khetan and Ors AIR1977 SC 536* are relevant to mention:-

*"...The mandatory character is strengthened by the negative form of the language. The prohibition against transfer without complying with the provisions of the Act is emphasised by the negative language. Negative language is worded to emphasise the insistence of compliance with the provisions of the Act. (See *State of Bihar v. Mahamjadbiraja Sir Kabemshwar Singh of Darbbhanga and Ors.* (1) MANU/SC/0019/1952 : [1952]1SCR889 K. *Pentiah and Ors. v. Mtiddala Veeramatlappa and Ors.* (2) MANU/SC/0263/1960 : [1961]2SCR295 and unreported decision dated 18 April, 1976 in *Criminal Appeal No. 279 of 11975 etc. Additional District Magistrate, Jabalpu v. Shivakant Shukla* (3). Negative words are clearly prohibitory and are ordinarily used as a legislative device to make a statutory provision imperative.*

*17. In Raza Buland Sugar Co. Ltd. v. Municipal Board (4) Rampur. (1965) 1 Section C.R. 970 this Court referred to various tests for finding out when a provision is mandatory or directory. The purpose for which the provision has been made, its nature, the intention of the legislature in making the provision, the general inconvenience or injustice which may result to the person from reading the provision one way or the other, the relation of the particular provision to other provisions dealing with the same subject and the language of the provision are all to be considered. Prohibition and negative words can rarely be directory. It has been aptly stated that there is one way to obey the command and that is completely to refrain from doing the forbidden act. Therefore, negative, prohibitory and exclusive words are indicative of the legislative intent when the statute is mandatory. (See Maxwell on Interpretation of Statutes 11th Ed. p. 362 seq; Cranford Statutory Construction, Interpretation of Laws p. 523 and Seth Bikharaj Jaipuria v. Union of India (5) MANU/SC/0045/1961 : [1962]2SCR880."*

10. In this case, FTIL has been alleged to be not 'fit and proper person' in view of the disqualification prescribed in regulation 20(1)(b)(v) of the SECC Regulations. In my view, as per provisions of this regulation, if any order against the concerned person, which has bearing on the securities market, has been passed by SEBI or any other regulatory authority, and a period of three years from the date of the order has not elapsed then that person will be disqualified to hold any shares in a recognized stock exchange and clearing corporation in view of prohibition contained in regulation 19 (1) of the SECC Regulations.
11. I note that in this case, the notice has spelt out the basis of the allegation and the applicable provisions of the SECC Regulations, the SCRA and the SEBI Act. The notice in para. 5 specifically states that as FMC has held FTIL not 'fit and proper person', in terms of provisions of regulation 20(1)(b)(v) of the SECC Regulations, it is not a 'fit and proper person' to acquire or hold shares of a recognized stock exchange or clearing corporation. The very reference to regulation 20(1)(b)(v) of the SECC Regulations in the notice indicates that the FMC order against FTIL has a bearing on the securities market.
12. I deem it necessary to mention here that during personal hearings in the matter on several dates, the authorised representatives of FTIL were explained that the SECC Regulations are not subservient to the quantum of shareholding of the concerned person in a recognised stock exchange or clearing corporation. It is his/her status which determines whether he/she is 'fit and proper person' or not in terms of regulation 20 of the SECC Regulations. They were further explained that it is obvious that if an order has been passed by a regulator of commodities market in the context of shareholding in commodity exchange, having similar function and obligation as those of a stock exchange, it will have a bearing on the securities market also since the person who is not 'fit and proper person' to hold shares in a commodity future exchange would also not be 'fit and proper person' to hold shares in the recognized stock exchange and clearing corporation, as both markets - commodity futures

market and the securities market require similar standards with regard market integrity, corporate governance, etc. They were given several opportunities to submit their response taking into account the same and also to explain their stand as to how the FMC order has no bearing on the securities market as contemplated under regulation 20(1)(b)(v) of the SECC Regulations. The dates of personal hearings were accordingly adjourned at the requests of the authorised representatives of FTIL. In response thereto, FTIL has made submissions that its shareholding in the recognized stock exchanges and clearing corporation is insignificant and as such it does not have any bearing on the securities market. I, therefore, do not agree with the contentions of FTIL that the notice does not spell out the basis or that FTIL did not have opportunity to submit its defence on whether the FMC order has bearing on the securities market. In view of the same, I find that the case does not require issuance of any supplemental notice and additional opportunity of personal hearing pursuant thereto as contended by FTIL.

13. With regard to submission of FTIL that it's less than 5% shareholding in MCX-SX and insignificant shareholding in other recognized stock exchanges and clearing corporation does not have bearing on the exchange, I find that the prohibition under regulation 19(1) of the SECC Regulations on a person, who is found to be not 'fit and proper person' in terms of regulation 20 of the Regulations, is not dependent upon the number or percentage of his/her shareholding or control in a recognized stock exchange or clearing corporation. It is also not dependent upon whether or not that person is represented in the board of directors of the recognized stock exchange or clearing corporation or he is person acting in concert with the management or board of directors of the recognized stock exchange or clearing corporation. The disqualification under regulation 20(1)(b)(v) of the SECC Regulations relates to an order of SEBI or any other regulatory authority which has a bearing on the securities market. If a person incurs such disqualification he cannot acquire or hold even one share in a recognized stock exchange or clearing corporation. I, therefore, do not find any merit in the submissions of FTIL in these respects.
14. Coming to the question whether the FMC order dated December 17, 2013 has a bearing on the securities market, I note that by this order, the FMC has "in the public interest" declared that FTIL is not a 'fit and proper person' to continue to be a shareholder of 2% or more of the paid-up equity capital of MCX. Such finding of the FMC has, in my view direct bearing on the securities market in light of the several factors such as:-
  - (a) Commodity future exchange and stock exchange basically discharge similar functions and obligations except that the two exchanges deal in different underlyings - physical

commodity being underlying in the commodity futures exchange and the securities being the underlying in the stock exchange.

- (b) Systems and processes such as trading platform, clearing and settlement are similar in both the markets. Settlement defaults in both the markets pose systemic risk to the respective markets.
  - (c) The regulatory objective in both the exchanges are same as far as investor protection, market integrity, transparency, fairness and governance are concerned.
  - (d) Both the markets are connected through substantial number of common stakeholders and flow of finance.
  - (e) Commodity future exchange as well as stock exchange and clearing corporation are Market Infrastructure Institutions of the financial markets needing the same level of integrity and governance standards.
15. In view of the above, a person who is not 'fit and proper' to hold shares in commodity future exchange cannot be a 'fit a proper person' to hold share in the recognized stock exchange and the clearing corporation. He poses same danger to the interest of securities market as to the commodity futures market as both the market require the same standard of integrity. Thus, there is no doubt that the declaration of FTIL as not 'fit and proper person' by FMC has direct bearing on the securities market. FTIL, therefore, has to be held not 'fit and proper' for holding shares in a stock exchange also in view of provision of regulation 20(1)(b)(v) of the SECC Regulations.
16. Accordingly, in terms of regulation 20(2) of the SECC Regulations, I hold that FTIL is not a 'fit and proper person' to acquire or hold, directly or indirectly, any equity shares or any instrument that provides for entitlement for equity shares or rights over equity shares at any future date.
17. Considering the facts and circumstances of the case, interest of investors and securities market, I do not find any reason to defer passing of this order or defer the implementation of this order as pleaded by FTIL.
18. I, therefore, in exercise of the powers conferred upon me under section 19 of the read with sections 11 and 11B of the Securities and Exchange Board of India Act, 1992 and section 12A of the Securities Contracts (Regulation) Act, 1956, read with regulations 20(2) and 49 of the Securities Contracts (Regulation)(Stock Exchanges and Clearing Corporations) Regulations, 2012, hereby issue the following directions:
- (a) FTIL is not a 'fit and proper person' to acquire or hold any equity share or any instrument that provides for entitlement for equity shares or rights over equity shares at

any future date, in a recognized stock exchange or clearing corporation, either directly or indirectly;

- (b) FTIL shall divest the equity shares and/or any instrument that provides for entitlement for equity shares or rights over equity shares at any future date, held by it, directly or indirectly, in MCX-SX, MCX-SX CCL, DSE, VSE and NSEIL within 90 days from the date of this order through sale of shares and /or instruments; and
  - (c) FTIL and the entities through whom it indirectly holds equity shares or any instrument entitling voting rights in MCX-SX, MCX-SX CCL, DSE, VSE and NSEIL shall cease to be entitled to exercise voting rights in respect of those shares or instruments, with immediate effect.
19. A copy of this order shall be served upon FTIL, MCX, MCX-SX, MCX-SX CCL, DSE, VSE and NSEIL to ensure compliance with above directions.

**Date: March 19<sup>th</sup>, 2014**

**RAJEEV KUMAR AGARWAL**

**WHOLE TIME MEMBER**

**Place: Mumbai**

**SECURITIES AND EXCHANGE BOARD OF INDIA**