

DELHI HIGH COURT

Rajesh Kumar Maheshwari

Vs.

Union of India, (Delhi)

Civil Writ No. 1838 of 1987. and C. M. No. 1801 of 1989

(Mrs. Leila Seth And V. B. Bansal, JJ.)

18.4.1990

JUDGEMENT

LEILA SETH, J.

1. The petitioner is a citizen of India and a graduate in commerce and law and has the requisite educational and professional qualifications to become a member of the Delhi Stock Exchange. He is praying for a writ of *certiorari* to quash the letter dated 5th February, 1987 written by the Government of India to the President of the Delhi Stock Exchange regarding increasing the membership and dilution of share holding of the said Exchange.

2. In order to appreciate the matter, it is necessary to set out the background of the case. The Delhi Stock Exchange Association Ltd. was incorporated on 25th June, 1947. The existing building was constructed in 1950 out of funds contributed by members. Initially, it was only necessary to hold one share to become a member but sometime in 1963 the eligibility criteria was changed to two shares. On 20th February, 1957, the Securities Contracts (Regulation) Act, 1956 (Act 42 of 1956) came into force. The object of the Act was to prevent in desirable transaction in securities by regulating the business of dealing therein, by prohibiting operations and by providing for certain other matters connected therewith. The Central Government granted recognition to the Delhi Stock Exchange under Section 4 of the said Act.

3. As the volume of work increased, the Delhi Stock Exchange sought the Government of India's permission to dilute every member's share-holding from two to one and admit as members authorized assistants etc. who had worked for a long period in the Stock Exchange. The Union of India, however, was anxious that the membership of the Delhi Stock Exchange be increased by induction of

members of the public generally.

4. On 8th January, 1986 a large number of the members of the Delhi Stock Exchange wrote to the Board of Directors indicating the enormous difficulties being faced by them because of the small size of the trading hall and expressing their fear that these difficulties would become more acute if the membership was increased. Consequently, they suggested that the increase in membership be done in a phased manner and a new building be constructed, further, members should be required to sell one of the two shares held by them.

5. Thereafter, on 31st January, 1986, the Delhi Stock Exchange Association Ltd. wrote to the Director (Investment) Stock Exchange Division, Ministry of Finance, Government of India stating that a detailed discussion had taken place regarding the difficulties experienced by members due to inadequacy of space in the existing building and the need to provide services to the increasing number of investors. With a view to providing better services to the investors and also keeping the interests of the existing members in mind, it was felt that the Articles "be amended to provide the eligibility of the membership of the Stock Exchange by holding one share". This would naturally increase the membership of the stock exchange from 125 to 250. It was further suggested that this increase should take place in a phased manner spread over three years in view of the space shortage. During this period, a member would be required to sell one share to another person "willing and otherwise eligible to become a member". It was also suggested that both the new member and the existing member would make a deposit of Rs. one lac each, resulting in a collection of Rs. 2.50 crores to be utilized in the construction of the new building. The Delhi Stock Exchange sought the approval of the Government of India to its proposal.

6. On 24th July, 1986, the Delhi Stock Exchange once again wrote to the Joint Secretary (Inv.), Government of India, regarding the intimation received for increase of membership of the Stock Exchange. It was indicated in the said letter that the Board was agreeable to the Government's suggestion regarding increase in membership and felt that hundred per cent increase would provide enough opportunity; further its proposal was already pending with Government, which if accepted, would increase the membership by hundred per cent. It referred to the limited space, which is not sufficient for more than hundred members, as being a constraint in the quick increase of membership.

7. A writ petition was filed by Mr. N. N. Saigal in the Supreme Court of India seeking a direction from the Government of India to permit and recognize a second stock exchange in Delhi. On 18th August, 1986 the Supreme Court of India passed the following order:

"Shri Anil Deo Singh learned counsel for the Union of India submits that steps will be taken to increase the membership of the Delhi Stock Exchange Association by 100% within 6 months. The learned Counsel has made the above statement on the basis of a letter received from the Delhi Stock Exchange Association Ltd. on 24-7-86. He prays that in view of the above submission the petition may be disposed of. We direct the Union of India to take necessary steps for increasing the membership by 100% within six months. We hope that the submission made on behalf of Union of India would be fully implemented within that period."

8. On 23rd September, 1986, the Delhi Stock Exchange once again wrote to the Joint Director, Stock Exchange Division. It stated that keeping in view the discussion held with the Joint Secretary (Investment), the Board reconsidered the matter and was now indicating the modified proposal. The proposal was that as mentioned earlier in the letter of 31st January, 1986, the qualification share for membership should be made one instead of two. Consequently, 125 shares would be available for increasing the membership. The existing members would then be free to dispose of their one surplus share, in a phased manner, within three years. The members disposing of their shares would be required to deposit a sum of Rs. one lac as security. 50 shares be offered directly to the public at a price to be determined by the Government and the amount to "go directly to the fund of the Stock Exchange" so that its resources are augmented "for construction of the new building". All this would naturally require amendment in the Articles of Association as also approval from the share-holders and the Government. As such, a request was made that the proposals be approved in principle, so that steps could be taken at the general meeting for approval and implementation.

9. On 12th November, 1986 the Government of India wrote a letter to the Delhi Stock Exchange. They referred therein to the letters of 31st January, 1986, 24th July, 1986 and 23rd September, 1986 on the subject of increase in membership. They indicated that the decision of the Government was that the membership must be increased to the extent of 150 shares by public issue of 300 shares.

Each share to be priced at Rs. 2,000/-; further the admission fee for each member should be Rs. 1 lakh instead of Rs. 1,000/- as prescribed in the Articles of Association and each new member be required to make "a non- interest bearing deposit of Rs. 3 lakhs for the new Building Fund and for the office space in the new building". The new members to be admitted on the basis of selection by objective criteria such as educational/professional qualifications, professional experience etc. It was also indicated in the said letter, that in the light of Civil Misc. Petition No. 11043/86 filed in Writ Petition No. 12233/85 by Mr. N. N. Saigal, there was a requirement to increase membership by hundred per cent by 18th January, 1987. This letter was written by the Director (Investment) who adverted to the fact that the Government had the power to withdraw the recognition granted to a stock exchange under the Securities Contracts (Regulation) Act, 1956 and directed the Delhi Stock Exchange to take immediate steps for increasing membership.

10. On 22nd December, 1986, the Delhi Stock Exchange wrote to the Director (Investment), Government of India and indicated that the matter had been discussed in the meeting of the Board of Directors held on 14th November, 1986 and informal meetings thereafter and reconsidered in the meeting held on 11th December, 1986. "Based on the assessment" of these meetings, it was proposed to pass a resolution "to increase the membership from 125 shares to 250 shares by amending the Articles of Association with regard to qualification share for becoming a member". Further, an extraordinary general meeting of the members of the Association was being convened for 6th January, 1987.

11. On 5th January, 1987 the Assistant Director, Stock Exchange Division wrote to the Delhi Stock Exchange Association Ltd. stating that the decision of the Board to reject the Government's directions of 12th November, 1986 to increase its membership by public issue and instead to get the approval of the General Body for splitting the existing shares so that the existing members could dispose of their surplus shares to the persons of their choice was contrary to the advice of the Government representatives and counter to the Government's intention to broad base the membership of the stock exchange. Consequently, it asked the governing body to show cause within ten days why it "should not be superseded in accordance with the provisions of Section 11 of the Securities Contracts (Regulation) Act, 1956 for non-compliance with Government's direction and having acted in a manner prejudicial to public interest".

12. On 15th January, 1987 the Delhi Stock Exchange wrote to the Secretary, Government of India, Ministry of Finance in response to the show cause notice. In the said letter it referred to the subsequent discussions held by some governing body member and other members of the Stock Exchange with Mr. P. G. Mankad, Joint Secretary. After giving the background of the correspondence, the difficulties envisaged with regard to space, valuation of property etc. and the directions of Government, the necessity of increasing membership, it submitted a proposal for consideration.

13. The proposal in brief was : that the membership be increased from 125 to 375. 125 members be added to the stock exchange by dilution of share holding of each existing member from two shares to one share and the share be offered preferably to authorized assistants, in the stock exchange at a price of Rs. 2 lakhs (Rs. 1 lakh as admission fee transferable and Rs. 1 lakh as interest free non-refundable transferable contribution towards building fund) to be deposited with the Stock Exchange. Another 125 members be added by public issue to be selected by a Committee. The new members would be required to pay Rs. 1 lakh as admission fee and Rs. 3 lakhs as interest free non- refundable deposit for building and other infra-structure etc. both transferable.

14. It was suggested that the proposal regarding "right shares to be given to the authorized assistants working in the Exchange for more than 2 years" merited consideration in view of the fact that sufficient experience had been gained by them and they had a preferential right to become members and render service to the public/investors. The reason for keeping their admission fee and deposit at half the value of the public issue was because of their experience and paying capacity. The valuation of the public issue shares and the higher non-refundable transferable deposit was suggested keeping in view the fact that the members of the Delhi Stock Exchange had built its own building from capital contributed by members before the Securities Contracts (Regulation) Act, 1956 came into force and before any listing fee income had accrued to the Stock Exchange.

15. The alternative proposal suggested was that the Memorandum and Articles of Association be amended "to increase the total of 125 shares by public issue without any rights etc. for the new members and ask to pay Rs. 10 lakhs as non-refundable transferable deposit with the stock exchange for building and other infrastructure facilities, having regard to the fact that the new member would have equal rights on the existing assets of the Association after becoming

members".

16. The permission, approval, consent etc. was sought from the Government expeditiously so that the Delhi Stock Exchange could implement and carry out the amendments, and the further increase of share-capital before 18th February, 1987.

17. On 5th February, 1987 the Government of India replied to the letter of the Delhi Stock Exchange dated 15th January, 1987. It stated that the proposals had been carefully considered and conveyed its approval regarding increase in membership subject to the certain conditions:

(i) The membership of the stock exchange be increased by 250 that is

(a) 125 members through public issue of shares; and

(b) 125 members through dilution of shareholding of each member from two shares to one share.

Necessary amendments in the Articles of Association of the Exchange be made in this regard.

(ii) All new members to pay an admission fee of Rs. 1 lakh.

(iii) New members admitted through public issue of shares and through dilution of existing shareholding to pay to the Stock Exchange an additional non-refundable deposit of Rs. 3 lakhs and Rs. 1 lakh respectively. These deposit amounts to be utilized by the Stock Exchange towards provisions of better infra-structure and services.

(iv) Selection of 250 members to be by objective criteria taking into consideration experience, professional qualifications and other relevant factors.

(v) Selection of new members to be by an Expert Committee.

(vi) The public issue of shares and the issue through dilution to be done simultaneously and completed within 3/4 months of receipt of letter.

(vii) The issue of shares through dilution of existing members be permitted only to Authorized Assistants of members of Delhi Stock Exchange, daughters/sons or direct dependents.

(viii) If extra share arising out of the dilution of share-holding is not disposed of within the stipulated period then no sole condition will prevail except for purposes already permitted.

The Delhi Stock Exchange was directed to take immediate action to increase the membership.

18. It appears that on 11th February, 1987 the Delhi Stock Exchange wrote to Government of India regarding some modifications in conditions (iii) and (vii). On 12th February, 1987 the Government replied to the said letter and approved the modification in condition (iii) that the deposit of Rs. 3 lakhs and Rs. 1 lakh be transferable but rejected the proposal of including successors or heirs of members in condition (vii) pertaining to issue of shares through dilution of existing members.

19. On 18th February, 1987 the Supreme Court of India passed the following order in Civil Writ Petition No. 12233 of 1985 filed by Mr. Saigal as also in Civil Misc. Petition No. 11043 of 1986 :-

"We are informed by the learned counsel for the Union of India that the Union of India has directed the Delhi Stock Exchange to increase its membership by 250 shares through a public issue of shares and dilution of shareholding of existing members from two shares to one share on a 50: 50 basis and that the necessary special resolution for increasing the membership would be passed by the Delhi Stock Exchange under Section 81 of the Companies Act within two months. The learned counsel also submits that within three months the shares of the Delhi Stock Exchange would be offered for public subscription in accordance with the resolution to be passed. In view of the above statement we find there is no need to proceed with the hearing of the Writ Petition.

The Civil Miscellaneous Petition and Writ Petition are disposed of accordingly."

20. On 10th June, 1987 the present writ petition was filed. The Union of India, the Director of Investments and the Joint Secretary, Stock Exchange Division were arrayed as respondents 1, 2 and 3. On 12th June, 1987 a show- cause notice was issued for 20th July, 1987 as to why the petition be not admitted and *ex parte* interim order was passed staying the operation of the letter dated 5th

February, 1987.

21. On 15th July, 1987 the respondents filed a reply and on 20th July, 1987 the interim order was extended and time was granted to file an affidavit in rejoinder. The matter was directed to be listed for further preliminary hearing on 17th August, 1987.

22. On 14th August, 1987 the Delhi Stock Exchange Association Ltd. moved an application being C. M. 3315/87 to be imp led as a party. On 17th August, 1987 this application was listed and was allowed as the court was of the view that the applicant was a necessary party. The reply filed by the applicant to the writ petition was taken on record and the petitioner was permitted to file a rejoinder, if he so wished.

23. On 2nd September, 1987, Rule. D. B. was issued. It was further directed that the hearing of the petition be expedited and in the meanwhile respondent No. 4, i.e. Delhi Stock Exchange could appoint an expert committee for the purpose of selection of new members and finalization of applications, but actual allotment be not made till the disposal of the petition. With respect to dilution of share-holding of each member from two shares to one share, it was directed that the applications received from existing members be processed but no transfer be effected till the disposal of the writ petition.

24. On an application, being C. M. 1304/88, moved by respondent No. 4, the order dated 2nd September, 1987 was modified on 23rd May, 1988, as applications from new members from the public had been received along with sums of Rs. 17,000/- as non-interest bearing application money and more than Rs. 2 crores applicants' money was lying unproductive. Since the Expert Committee had made its recommendations but the report had not been submitted to respondent No. 4, in view of the order of the court, the court permitted respondent No. 4 to proceed with the selection of new members but not to allot any shares to the newly selected members. Respondent No. 4 was also permitted to return the money of the applicants whose applications had been finally rejected.

25. Subsequently, an application was moved, being C. M. 1801 of 89, by the selected persons for being imp led as parties. On 25th August, 1989 counsel for the petitioner suggested that the applicants in C. M. 1801/89 be heard on the writ petition on merits. We ordered accordingly.

26. It is in this background that we have to examine the contentions of learned counsel for the petitioner and respondents.

27. Learned counsel for the petitioner contends that the directions contained in the impugned order dated 5th February, 1987 issued by the Central Government are arbitrary, illegal and void. He submits that the said directions/approvals are discriminatory, prejudicial to public interest and contrary to the policy of the Government to broad base membership of the Delhi Stock Exchange.

28. The argument appears to be that permission to members of the Delhi Stock Exchange to transfer their surplus share to their authorized assistants etc. is illegal and it should have been mandatory that the dilution be by way of transfer to members of the general public. Further, the difference in the amounts to be paid by way of deposit by the members of the public as compared to transferees of shares by dilution is discriminatory. Apart from this, it is urged that this is contrary to the commitment made to the Supreme Court in N. N. Saigal's case referred to above. It is also contended that the inclusion of Directors/Members of the Delhi Stock Exchange in the Expert Selection Committee is violative of Article 14.

29. It appears to us that the argument regarding discrimination is not tenable. It is well settled that to sustain a plea of discrimination, it is essential to establish that all persons dissimilarly treated constitute a homogeneous class. In the present case, members of the public and authorized assistants of members of the Delhi Stock Exchange do not constitute a homogeneous class. The classification is based on the fact that persons who have been working over the years in the Stock Exchange have acquired a certain expertise as compared to the general public and, therefore, they constitute two different groups. We are fortified in our view by the decision of the Supreme Court.

30. In *Madhubhai Amathalal Gandhi v. Union of India*,¹ a notification imposing, inter alia, a condition that members of the Indian Stock Exchange Ltd., would be entitled to apply for membership of the Stock Exchange, Bombay provided they were active members for twelve months immediately preceding 6th August, 1957, was challenged as discriminatory. It was urged that classification of members into two groups, one active and the other non-active was arbitrary and had no reasonable relation to the object sought to be achieved.

31. Mr. Justice K. Subba Rao speaking for the Court observed that a

classification must have a reasonable relation with the object sought to be achieved; the standard of reasonableness being inextricably conditioned by the extent and nature of the evil and the urgency for eradicating the same. The object of the notification dated 31st August, 1957 issued under Section 4 of the Securities Contracts (Regulation) Act, 1956 is two-fold. The main object being to carry out the purpose of the Act, namely, to prevent undesirable transactions in securities by regulating the business in them" and the subsidiary object being to "assuage the hardship that recognition of only one stock exchange would cause to the members of the other association". It is to achieve this twin object that the classification has been made between active and inactive members. On one hand Government found it necessary to exclude nominal members who would add their deadweight to the recognized association and bring down its efficiency and affect its disciplined conduct of business, on the other hand it gave an opportunity to persons who were actively interested in the business to become regular members of the Stock Exchange, Bombay. On a consideration of the necessary data and presumably having regard to the record of activities of various members, the Government fixed, the activities in the crucial year 1956-57 as the standard of activity for membership and fixed 12 months immediately preceding 6-8-1957 as standard for active membership. There is a presumption in favor of the State that there is a reasonable basis for the classification. Consequently the Supreme Court held that the notification was not discriminatory and the period fixed by the Government as the standard for ascertaining the active membership is not arbitrary or unreasonable.

32. Taking a cue from the above mentioned case it is apparent that the object of the Central Government in granting the approval by its letter dated 5th February, 1987 was clearly to provide adequate facilities to the investors as a result of the increased volume of work and to broad base the Stock Exchange membership without totally depriving the existing members of their rights.

33. Admittedly, authorized assistance are persons who have worked and gained experience over the years in the Stock Exchange. This experience will certainly benefit the investors and making such persons members is in public interest. Even under the Articles of Association of the Delhi Stock Exchange

it is those persons who are eligible to be admitted as members (see Article 25(2)(a)). Though this condition can be waived by the Board of Directors on certain conditions, actual waiver is necessary. We are not aware of any law

which compels existing members to transfer their share-holding to the public generally. The existing members are full owners and are perfectly entitled to transfer their shares to persons of their choice. In any case, as noticed above, the public is being benefited by the fact that the authorized assistants are well versed in their work and the existing members are not passing their preferential rights under Section 81 of the Companies Act. Consequently, the induction of authorized assistants etc. as members on transfer of the surplus share by existing members appears to be a reasonable classification.

34. The object of dilution is different from the object of the public issue as in the first case it is to make provision for admission for existing authorized agents whereas in the latter case it is to admit members of the public generally. As such, a claim that members of the general public be treated at par for the purpose of deposit with those persons inducted at the request or behest of existing members is not sustainable. The public issue is without any premium being charged though admittedly the real value of the share far exceeds its face value as the company owns very valuable property.

35. The Supreme Court in *Narendra Kumar Maheshwari v. Union of India*,² held that there is no reason why a company should not structure its issue in a manner that it confers greater advantages and benefits on existing shareholders and promoters.

36. In this view of the matter the difference in the amount of deposit is totally consistent with the respective objects sought to be achieved.

37. From the background of the case, as above indicated, it is apparent that the members of the Delhi Stock Exchange were seeking permission to dilute their holding and admit their authorized assistants etc. as members whereas the Government was anxious to increase membership by induction of the public generally. The filing of the writ petition in the Supreme Court and the correspondence between the Government and the Stock Exchange putting forward their respective points of view, has been set out above. It appears that eventually a package deal was agreed to under which the Delhi Stock Exchange's proposal to permit dilution was accepted along with the Government's request to have a hundred per cent expansion. That is why the Government gave its assent to the two independent transactions i.e. the admission of 125 authorized assistants etc. by transfer of the surplus share held

by the existing members and the induction of 125 members of the public so that there is a hundred per cent expansion of the existing membership strength, as envisaged in the order of the Supreme Court dated 18th August, 1986, thus making a total of 375 members and broad basing the organization. The two transactions are separate, one is the issue of 125 shares to the members of the public on certain terms and conditions and the other is the permission to existing members to dilute their holding by transfer of one share to their authorized assistants etc. It is not correct to challenge the two independent transactions on the ground that the terms of the two components do not coincide. As indicated above, members of the public seeking membership and authorized assistants etc. becoming members on transfer of surplus share of existing members do not belong to the same homogeneous class.

38. It, therefore, appears to us that the dilution by way of transfer of existing shares in favor of authorized assistants etc. is valid and in accordance with the assurance given to the Supreme Court. The said assurance was that there would be a hundred per cent expansion in favor of the members of the public. There were 125 members and 125 members are to be taken from the public. The induction of another 125 members by dilution cannot be considered arbitrary in view of the facts indicated above, especially as this is limited to authorized assistants etc. who are coming in or transfer of surplus shares of the existing members. It is pertinent to note that the impugned letter of Central Government is dated 5th February, 1987 i.e. prior to the passing of the order in the Supreme Court in N. N. Saigal's case on 18th February, 1987. The order of the Supreme Court reflects the Central Government directions to the Delhi Stock Exchange both with regard to public issue as also dilution of existing membership. Consequently, the contention that the said letter is contrary to the commitment made to the Supreme Court is not sustainable.

39. The next submission relates to the personnel of the Expert Selection Committee. The said Committee constituted for induction of new members, consists of some members of the Board of Directors and nominees of the Government and public representatives. Under the Memorandum and Articles of Association, the selection of members is purely by members of the Board of Directors of the Delhi Stock Exchange. The validity of this condition in the Memorandum of Articles of Association is not under challenge. Consequently, it is difficult to appreciate how the constitution of the Expert Selection

Committee becomes arbitrary when some of its members are Directors of the Board of the Delhi Stock Exchange. It is also pertinent to note that the selection of members by this Committee is to be done on the basis of an objective criteria taking experience, professional qualification and other relevant factors into consideration. We, therefore, find that the constitution of the Selection Committee comprising partly of members of the Board of Directors of the Stock Exchange is not violative of Article 14.

40. Learned Counsel for the petitioner made certain oral submissions pertaining to the action of the Delhi Stock Exchange and violation of provisions of the Securities Contracts (Regulation) Act, 1956.

41. As noticed above, the petitioner filed the writ petition challenging only the action of Government as contained in its letter dated 5th February, 1987 and made only the Union of India and its two officers parties. The Delhi Stock Exchange was not made a party. However, the Delhi Stock Exchange moved an application to be imp leded and it was only on 17th August, 1987 that it was imp leded as respondent No. 4. There are no pleadings in the writ petition challenging any action of the Delhi Stock Exchange nor in any relief sought. Consequently, we do not think it necessary to deal with these submissions.

42. For the reasons outlined above, we discharge the rule. However, in the facts and circumstances of the case, we make no order as to costs.

Order accordingly.

Cases Referred.

1. AIR 1961 Supreme Court 21,
2. AIR 1989 Supreme Court 2138,