Demutualisation of Stock Exchanges

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An expert committee appointed by SEBI has recently recommended demutualisation of stock exchanges since stock exchanges, brokers associations and investors association have overwhelmingly felt that such a measure was desirable. The committee has accordingly suggested the steps for such demutualisation. This article examines and explains the concept of demutualisation and its implications and concerns.

"MUTUAL" VERSUS "DEMUTUAL"

HISTORICALLY stock exchanges were formed as 'mutual' organizations, which were considered beneficial in terms of tax benefits and matters of compliance. They are generally "not-for-profit" and tax exempted entities. The trading members who provide broking services, also own, control and manage such exchanges for their common benefit, but do not distribute the profits among themselves. The ownership rights and trading rights are clubbed together in a membership card which is not freely transferable and hence this card at times carries a premium. In contrast, in a "demutual" exchange, three separate sets of people own the exchange, manage it and use its services. The owners usually vest management in a board of directors which is assisted by a professional team. A completely different set of people use trading platform of the exchange. These are generally "for-profit" and tax paying entities. The ownership rights are freely transferable. Trading rights are acquired / surrendered in terms of transparent rules. Membership cards do not exist. These two models of exchanges are generally referred to as "club" and "institution" respectively.

Stock exchanges frame and enforce rules, which may not always, further the public interest (interest of investors and society) and the private interest (interests of trading members) simultaneously. Theoretically public interest gets precedence in a demutualised exchange while private interest gets precedence in a mutual exchange in the formulation and implementation of the rules. In a mutual exchange, the brokers elect their representatives to regulate the activities of the exchange, including their own activities. As a result, in case of a dispute between brokers and the investors, investors' interests do not always receive the same utmost objective treatment. The regulatory and public interest role of the exchange gives way to private interests of the elected directors. As the self sometimes gets precedence over regulation, mutual exchanges do not offer an effective model for self-regulatory organisations.

On realising the limitations of mutual structure and discovering the advantages of demutual structure, the stock exchanges are increasingly organising themselves as commercial entities and undergoing a process of "demutualisation". The Group on Corporatisation and Demutualisation of Stock Exchanges appointed by SEBI summarises the arguments in favour of demutualisation as follows:

- "Stock exchanges owned by members tend to work towards the interest of members alone, which could on occasion be detrimental to the rights of other stakeholders. Division of ownership between members and outsiders can lead to a balanced approach, remove conflicts of interest, create greater management accountability, and take into consideration the interest of other players.
- To cope with competition, stock exchanges require funds. While member owned stock exchanges have limitations in raising funds, publicly owned stock exchanges can tap capital markets.
- Publicly owned stock exchanges can be more professional when compared to member owned organizations. Further, as a result of the role played by shareholders, strengthening of the management and the organization, there is greater transparency in dealings, accountability and market discipline.
- This would enhance management flexibility. A publicly held company is better equipped to respond to changes when compared to a closely held mutually owned organization. Further, a company can spin off its subsidiaries, get into mergers and acquisitions, raise funds, etc."

The concept of demutualised exchange most probably originated in India, where two exchanges (OTCEI in 1990 and NSE in 1992) adopted pure demutualised structure from their birth. The Stockholm Stock Exchange was the first major stock exchange in the world to become demutualised in 1993. Since then, over 20 exchanges have demutualised. Some of them like Australian Stock Exchange, London Stock Exchange, and Singapore Stock Exchange have gone one step further by becoming a listed company. Many others, including commodity exchanges, are in the process of demutualisation.

HISTORICAL BACKGROUND

There are 23 recognised exchanges in the country. Three of them are "Association of Persons", while the balance 20 are companies, either limited by guarantee or by shares. Except one exchange (NSE), all exchanges, whether corporates or association of persons, are not-for-profit making organizations. Except for two (OTCEI and NSE), all exchanges are "mutual" organisations.

The limitations of a mutual structure has been realised time and again by the exchanges and the regulators. In early 1980s, the High Powered Committee on Stock Exchange Reforms had observed: "There is considerable disillusionment in the country with the functioning of the Governing Bodies. It is alleged that most of the stockbrokers have vested interest in maintaining the status quo as they have their own self-interest to protect. They also at times subordinate the interest of the genuine investors to those of the stockbrokers. Some of them are even alleged to have misused their position of trust for personal gains. They often fail to take disciplinary actions against erring members and allow crisis situations to develop in the Stock Exchanges by neglecting to take timely action to curb excessive speculation. The measure which they adopt, at times, for regulating business are either half-hearted or not implemented rigorously." The Committee recommended amendments in law to enable the government to change the organisation form of stock exchanges, which were then association of persons or companies limited by shares so that all the stock exchanges had an uniform organisational structure as companies limited by guarantee. It also recommended that at least 50% of the board members should be outside directors comprising of professionals, industrialists, financial experts, nominees of government and representatives of investor associations. The High Powered Study Group on Establishment of New Stock Exchanges in early 1990s reiterated these recommendations. In 2002, the Group on Corporatisation and Demutualisation of Stock Exchanges also reiterated that most stock exchanges have failed to develop good corporate governance practices and strong management teams... Conflicts of interest have bedeviled the operations of the stock exchanges in the past to the detriment of the securities market.

Reforms initially focused on reducing dominance of trading members in the management of stock exchanges by prescribing composition of governing council and strengthening the position of executive director. SEBI forced the exchanges in 1993 to reconstitute their governing councils to provide for at least 50% non-broker representation. Since then 21 exchanges in the country are being managed by governing councils comprising of elected trading members and nominees of SEBI (SEBI Nominees and Public Representatives) in the ratio of 50:50. By taking into account the executive director, who is supposed to be independent, non-broker members out number broking members in the councils.

This did not materially alter the situation. The composition of governing council is only theoretically a 50:50 ratio between brokers and non-brokers, while in practice the composition is titled in favour of brokers. This is mainly because: (a) broker-directors, who have considerable hand in the choice of public representatives, may not choose independent persons or persons critical of brokers, (b) many of the non broker-directors, while distinguished in other walks of life, do not often understand the intricacies of functioning of stock exchanges and are not assertive enough nor very regular in attending meetings, and (c) the office bearers (President, Vice President etc.) of the governing council are the broker-directors, who dominate the show. It is not unusual for many non-elected directors to espouse directly or indirectly the interest of the brokers during the deliberations in the council, since they owe their nomination to the elected directors. On the other hand, the elected directors, who attend every meeting of the council, develop a coordinated approach in articulating their group interest. The obliging nominees facilitate them in achieving their group interest, which may be to the detriment of other participants.

The exchanges, therefore, witness different types of crises from time to time. A post-mortem of these has generally revealed the complicity of elected directors. The investigations into the massive rigging in prices of certain scrips during May-June 1998 revealed a number of systemic deficiencies including the composition of governing councils. It was felt that the 50:50 composition should be replaced by 40:60 to reduce dominance of elected directors in decision making. Non-brokers should be allowed to become president. A "code of ethics" could be prescribed requiring broker-directors, who are office bearers of stock exchanges, not to do proprietary trading while holding office. Before these systemic improvements could be affected, the market witnessed a massive crisis in early 2001 involving some brokers and the banking system. Though the investigations are on, preliminary findings indicate complicity of elected directors.

The above analysis leads to the inevitable conclusion that the quality of administration of broker-managed exchanges is far from satisfactory. And the tinkering attempts (composition of governing council and strengthening of position of executive director) made for decades to improve the working of the exchanges while retaining the basic structure has not yielded any appreciable result. In order to address the malaise, the Finance Minister in March 2001 proposed corporatisation of stock exchanges by which ownership, management, and trading membership would be segregated from each other. In order to promote demutualisation of stock exchanges, the Finance Act, 2001 amended the Income tax Act, 1961 to provide that any transfer of capital asset (not all assets) from an association of persons or body of individuals to a company in the course of corporatisation of a recognised stock exchange shall not be regarded as transfer for the purposes of capital gains tax. This one time exemption from capital gains is available only if all the assets and liabilities of the stock exchange immediately before the succession become assets and liabilities of the corporatised stock exchange, and the corporatisation is carried out in accordance with the scheme of corporatisation approved by SEBI. It also provided that for the purpose of computation of capital gains, the cost of equity shares allotted to shareholders under the scheme of corporatisation shall be the cost of acquisition of his original membership. SEBI directed the exchanges in May 2001 to amend their byelaws to provide for adoption of a Code of Ethics for their directors. This required the elected office bearers to refrain from proprietary trades in securities, directly or indirectly, during their tenure. SEBI also directed the exchanges in January 2002 to suitably amend their Rules, Articles etc. to provide that no broker member of the stock exchanges shall be an office bearer of an exchange, i.e. hold the position of President, Vice President, Treasurer, etc. The Finance Minister reiterated in his Budget Speech for the year 2002-03 that the process of demutualisation would be completed during the course of the year to implement the decision to separate ownership, management and operation of the stock exchanges.

GROUP ON DEMUTUALISATION

Since demutualisation is a complex issue, SEBI constituted a Group under the Chairmanship of Justice M. H. Kania, former Chief Justice of India to advise SEBI on the matter and to recommend the steps to implement the demutualisation. The Group observed that the stock exchanges, representatives of broker's associations and investors' associations were unanimous on the desirability of demutualisation and made the following recommendations:

(i) A common model for corporatisation and demutualisation may be adopted for all stock exchanges. Each stock exchange would be required to submit a scheme drawn on the lines of the recommendations of the Group to SEBI for approval. Any stock exchange failing to comply with the requirement of corporatisation and demutualisation by the appointed date may be derecognised.

(ii) The SCRA may be amended to provide that a stock exchange should be a company incorporated under the Companies Act. The stock exchanges set up as association of persons or as companies limited by guarantee may be converted into companies limited by shares.

(iii) The Income tax Act may be amended to provide that the accumulated reserves of the stock exchange as on the day of corporatisation are not taxed. The reserves may be taxed in the hands of the shareholders when these are distributed to shareholders as dividend at the net applicable tax rate. All future profits of the stock exchange after it becomes a for-profit company may be taxed. Further, the issue of ownership rights (shares) and trading rights in lieu of the card should not be regarded as transfer and not attract capital gains tax. However, at the point of sale of any of these two rights, capital gains tax would be attracted.

(iv) The Indian Stamp Act and the Sales Tax laws may be amended to exempt from stamp duty and sales tax, the transfer of the assets from the mutual stock exchange and the issuance of shares by the new demutualised for-profit company.

(v) While the Group favours the deposit system for trading rights, it likes to leave the choice of adopting either the card or the deposit system to the exchanges. If the deposit system is accepted, the value of the card will be segregated into two independent rights namely the right to share in the net assets and goodwill of the stock exchange and the right to trade on the stock exchange.

(vi) The three stakeholders viz. shareholders, brokers and investing public through the regulatory body should be equally represented on the governing board of the demutualised exchange. The roles and hence the posts of the Chairman and Chief Executive should be segregated. The Chairman should be a person who has considerable knowledge and experience of the functioning of the stock exchanges and the capital market. The Chairman of the Board should not be a practising broker. The exchange must appoint a CEO who would be solely responsible for the day to day functioning of the exchange, including compliance with various regulations and risk management practices. The board should not constitute any committee which would dilute the independence of the CEO.

(vii) The demutualised stock exchanges should follow the relevant norms of corporate governance applicable to listed companies in particular, the constitution of the audit committee, standards of financial disclosure and accounting standards, disclosures in the annual reports, disclosures to shareholders and management systems and procedures. It would be desirable for a demutualised exchange to list its shares on itself or on any other exchange. However, this may not be made mandatory; in case the exchange is listed the monitoring of its listing conditions should be left to the Central Listing Authority or SEBI.

(viii) No specific form of dispersal need be prescribed but there should be a time limit prescribed, say three years which can be extended by a further maximum period of 2 years with the approval of SEBI, within which at least 51% of the shares would be held by non-trading members of the stock exchange. There should be a ceiling of 5% of the voting rights which can be exercised by a single entity or groups of related entities, irrespective of the size of ownership of the shares.

NSE MODEL OF DEMUTUALISATION

Fortunately, Indian securities market has tasted the benefits of demutualisation. Two newly set up exchanges, namely, NSE and OTCEI, are managed by boards of directors, which do not include trading members. From day one, these have been the purest form of demutualised exchanges where brokers do not own the shares and the management is free from broker control. The ownership, management and trading on these two exchanges are in the hands of three different sets of people. This has completely eliminated any conflict of interest and helped NSE to pursue market efficiency and investors' interests aggressively. Though crises have been hitting the stock market at regular intervals, NSE emerges unscathed every time. This proves that absence of brokers in the governing council or having a governing council consisting of professionals only brings about more efficiency and transparency in the working of an exchange.

NSE model, however, does not preclude, rather accommodates broker involvement, support and contribution in a variety of other ways. It's board comprises of senior executives from promoter institutions (leading financial institutions), eminent professionals, nominees of SEBI and a full time executive. While the board deals with broad policy issues, the executive committee (EC), which includes trading members, formed under the Articles of Association and Rules, manages the day-to-day affairs of the exchange. The EC has constituted several other committees, like Committee on Trade Related Issues (COTI), Committee on Settlement Issues (COSI), which mostly consist of trading members and provide regulatory inputs from market.

The NSE model of demutualisation compares well with the international models of demutualised stock exchanges, as may be seen from Table 1. NSE model has two non-overlapping sets of people as trading members and shareholders, while international models permit such overlap. The former model has no ceiling on the holding of a shareholder, while the latter model generally has a ceiling.

TABLE 1: **NSE Model and the International Models of Demutualised Stock Exchanges**

Comparators	*International Model*	*NSE Model*
Legal Structure	Company	Company
For Profit/Not for Profit	For Profit Company	For Profit Company
Ownership Structure	Owned by Shareholders which includes brokers	Owned by Shareholders which are financial institutions which also have broking firms as subsidiaries.
Listing	Several stock exchanges are listed on themselves after Initial Public Offer.	Not a listed company. No Initial Public Offer made.
Ceilings on shareholding	Mostly 5% of voting rights for a single shareholder	No ceiling
Segregation of ownership, trading rights and management	These are segregated. To become a member of the demutualised stock exchange, it is not necessary to own a share in the company. Thus, members may or may not be shareholders and members who own shares may sell off their trading rights and all shareholders are not necessarily members.	These are segregated. The trading rights and ownership are segregated. The broking firms are not shareholders.
Board Structure	The Governing Board comprises of directors who are elected by shareholders. Some of the directors are brokers but majority do not have stock broking background.	The Board comprises of representatives of shareholders, academics, chartered accountants, legal experts etc. Of these, 3 directors are nominated by SEBI and 3 directors are public representatives approved by SEBI.
Fiscal benefits	As mutual entities, stock exchanges enjoyed fiscal benefits prior to demutualisation, but when converted into for profit companies these are taxed.	NSE was set up as a demutualised for profit company and is taxed. So the question of fiscal benefit prior to demutualisation does not arise.
Transfer of assets	Assets were transferred from the mutual entity to the for-profit demutualised company and shares were given to the members in lieu of the ownership in the old entity. There was no cash consideration paid. Since an Initial Public Offer (IPO) was also made in many cases, the valuation of the shares were done by the market and no separate valuation exercise was required as for example in the case of LSE where a bonus issue was made.	The question of transfer of assets did not arise because NSE was set up by the institutions as a demutualised company itself.
Enactment of legislation to give effect to demutualisation	In several countries a separate legislation was necessary as in the case of Australia, Hong Kong, Toronto and Singapore. In several others no legislation was necessary as in the case of UK.	Not applicable as NSE was set up as a demutualised company.

Source: *Report of the SEBI Group on Corporatisation and Demutualisation of Stock Exchanges.*

CONCERNS IN DEMUTUALISATION

Successful demutualisation requires us to be aware of the following concerns (Sahoo, 2001):

- A "demutual" suffers from a different type of conflict of interest. Since it is a "for-profit" organisation, its commercial role may get precedence over the regulatory role. Every decision is likely to be tested against its impact on profitability. It may, for example, be either very lenient in enforcing the rules to encourage the volume of business or very strict in enforcement of rules to increase penal revenue. This may require the regulator to take over some of the critical regulatory functions from the exchanges. NSE has, however, been able to strike a fine balance between its commercial and regulatory roles, which supplement each other.
- A demutualised exchange may like to be listed on an exchange. This would open up another arena for conflict of interest if it listed on itself as has the Australian exchange done. It is unlikely that the exchange would like to subject itself to same strict discipline as applicable to other listed companies. One solution could be to list the securities on another exchange, but permit trading on itself. A better solution would be to vest the listing powers in a body, like UK Listing Authority, separate from stock exchanges.
- In a mutual environment, the governing councils include

nominees of regulators and public representatives. This is necessary in public interest to refrain the elected directors from pursuing their self-interest only. In the demutualised environment, such a check is also necessary to ensure that the board of directors do not act only in the best commercial interest of the organisation. This may be achieved by including a few public representatives, who should have specific responsibilities and be held accountable.

The practice of having nominees of regulator must, however, be discontinued. This makes regulator vicariously liable for all the crises occurring in exchanges. The regulator cannot exonerate itself that the crisis is due to some lapse on the part of the exchange. Further, the regulator cannot be expected to make, at least in theory, a fair investigation into the affairs of the exchange, which is managed by it. Regulator should retain its regulatory role only and give up its role as management of the exchanges.

- It is an undenying fact that a "mutual" has better access to expertise and knowledge of the market participants, which are critical inputs for framing rules. As the brokers are involved in framing the rules, a "mutual" generally ensures better compliance with such rules by them. The access to market expertise and knowledge and compliance with the rules have been successfully achieved by NSE through EC, COSI, COTI etc.
  - In the demutual environment, the shares can be cornered by a few or undesirable persons. The exchanges could be prone to hostile takeovers. Such probability can be reduced by prescribing ceiling on shareholdings and requiring regulator's approval for change in ownership beyond a threshold limit. Public representatives would be useful to prevent mismanagement in such cases.

ISSUES IN DEMUTUALISATION

While evolving and implementing a scheme of demutualisation, the authorities need to pay attention to the following aspects:

- By demutualisation, the authorities seem to be suggesting separation of ownership, management and operation of the exchanges. It may mean that three different sets of people will have ownership, management and trading rights, as in case of NSE. It may also mean that the same set of people will have these three cleanly segregated rights, not just membership rights which camouflages all three rights. In the former case, the existing members have to decide to retain either ownership rights or trading rights, not both simultaneously. In the latter case, they have to decide if they would like to retain both the rights. If a member chooses to retain both the rights, i.e. the same person owns shares in the exchange and also trades on the exchange, he will have only economic (not political) rights associated with ownership. In respect of ownership rights, he should be debarred from joining governing board.
- It is most desirable if the initiative for demutualisation comes from the exchanges themselves. The exchanges should submit a scheme of demutualisation for approval. SEBI should just approve the scheme as they did for NSE or OTCEI at the time of their recognition. What if they do not demutualise voluntarily? The law provides enough stick for the authorities to enforce demutualisation. They have powers to recognise a stock exchange, renew the recognition or withdraw recognition in the interest of trade and/or in public interest. As a condition of recognition/renewal of recognition, a stock exchange is required to comply with such conditions as are or may be prescribed or imposed under the provisions of the SCRA and the SCRR from time to time. Besides, the authorities have powers to direct stock exchanges to make rules or to amend rules. In the extreme case of non-compliance by any stock exchange, the authorities can withdraw recognition.
- The SCRA permits different structures for stock exchanges. That is why some exchanges are associations of persons, some are companies limited by shares, and some others are companies limited by guarantee. Since the law permits any form for a stock exchange, it may not be possible to mandate a particular form for all exchanges. Hence law may have to be amended to specify that only companies limited by shares can be a stock exchange. Since amendment of law is a very time consuming process, it may inordinately delay demutualisation. However, it may be noted that the SCRA is a skeleton legislation under which regulators and SROs have substantial delegated powers of legislation. Under the delegated powers of legislation, the regulators can specify and enforce a particular structure. The exercise of powers described in the last paragraph would also enable regulators to mandate a particular structure. Even without all these, we have two demutualised exchanges.
- The corporatisation-cum-demutualisation would result in two classes of members namely, trading members and shareholder-members. Since "member" under the SCRA means a member of the recognised stock exchange, it is apprehended in some circles that the SCRA may not accommodate different classes of members. Again, NSE model, which has these two types of members, provides the solution. It has been affirmed recently by the Supreme Court (2001) that there can be more than one class of members and they will fall within the definition of "members" under the SCRA. Hence no amendment in SCRA is required.
- The process of demutualisation would involve offering shares of a corporatised exchange to public, including trading members. It is possible that the trading members subscribe for the shares and in terms of their rights under the Companies Act, get themselves elected to the board of directors. This defeats the purpose of demutualisation. It would then be necessary to specify under the SCRA that a shareholder, who is also a trading member, can not join the board. There is thus an apparent conflict between the Companies Act and the SCRA in the sense that the former confers a right on the shareholder to join the management while the later deprives a broker-shareholder from joining the management. This conflict is easily resolved by the well-accepted principle that the special law (SCRA) prevails over the general law (Companies Act). A deep understanding of the laws, however, overshadows this conflict and makes it clear that both the Acts are seeking to fulfill the same objective. The Companies Act requires an interested director to refrain from participating in the deliberations in the board meetings. Since a broker-shareholder, if elected to board of directors of an exchange, would be a perpetually interested director, he has to refrain from attending the board meetings and hence can not really contribute to management. It is, therefore, desirable that such a shareholder refrains voluntarily from joining the board or is prevented from joining

the board by the SCRA. Thus the SCRA would reinforce the objective of the Companies Act more explicitly.

- In case an exchange is to be corporatised and demutualised, it would involve transfer of assets and liabilities from the erstwhile mutual (non-corporate) exchange to the emerging demutual (corporate) exchange. Since this transfer is a notional transfer on conversion of the exchange from mutual to demutual form, and it is in public interest, the transfer of capital assets has been exempted from capital gains tax. The demutual exchanges would also inherit the accumulated reserves and surplus which has grown because of so many concessions and tax benefits. Since this remains with the organization even after conversion and is not taken away by any body, this should not be taxed. However, there should be a restriction on distribution of this accumulated reserve and surplus inherited by the demutual exchange, as these belonged to erstwhile not-for-profit exchange. This means that the exchange should continue to have the non-distribution clause prohibiting distribution of profits/dividends out of the inherited reserves and surplus. This is necessary in view of a 1997 judgment of the Supreme Court that income tax exemption is available only for those assessment years when rules of the exchange contain a provision prohibiting distribution of profits/dividends to its members. Hence, the exchange would be corporatised and demutualised, but continue to be a not-for-profit organisation. This reserve and surplus should be deployed by the exchange separately for common benefit of investors/exchange/market. Or, if the exchange becomes a for-profit organization, the reserve and surplus should be capitalised and issued as equity shares to government (representing all stake holders) which can disinvest in due course and all future profits of the organization should be subject to normal taxation.
- Demutualisation contemplates clean segregation of the membership card into two separate rights, namely trading rights and ownership rights. It has, however, to borne in mind that the membership card of a stockbroker is not a right/ property; it is a personal privilege to trade on the exchange (Supreme Court, 2001). If this has to be segregated into two separate rights, an overriding provision in the statute is required. Further, the value of membership card has to be determined by dividing the fair value of the exchange by the number of cards. For this purpose, the fair value of the exchange should exclude accumulated reserve and surplus, which belong to the exchange only. Otherwise, it would amount to distribution of profits, which is prohibited. The fair value should also exclude the deposits taken from members towards exposure, as they would continue to have trading rights against the deposits. As the exchanges lose club character, trading rights would have zero value and it can be acquired / surrendered freely subject to capital adequacy requirements. The amount of deposits would only determine the level of exposure and would vary from time to time depending on risk management mechanism in place. In respect of the trading rights, the brokers should not be subject to any taxation, as there is no transfer / acquisition of assets/ rights. Against the deposit with the mutual exchange, they would have trading rights on the demutual exchange. In lieu of membership card, the existing brokers should be granted transferable ownership rights (equity shares). This should also not be taxed. Otherwise, demutualisation would be penalty on them; in the absence of demutualisation, they would continue to enjoy trading and ownership rights without any tax liability. However, when they transfer ownership rights, they would be subject to capital gains tax and the cost of these rights shall be the cost of acquisition of the original membership. Further, all transactions associated with corporatisation and demutualisation should be exempted from stamp duty as this is done in public interest.

Assume that the fair value of an exchange is Rs. 250 crore, it has Rs. 100 crore of reserves and surplus and Rs. 100 crore of deposits obtained from members and it has 100 members. The entire Rs. 250 crore will be transferred to the emerging demutual exchange. Rs. 100 crore of reserve and surplus would be equitised and allotted to Government. Against Rs. 100 crore of deposit, members would continue to have trading rights. The balance Rs. 50 crore will be capitalized and issued as equity shares to 100 members against their membership card. At the time of demutualisation, no transaction shall attract any tax liability.

- The Group on Demutualisation seem to be suggesting only corporatisation of the exchanges, not demutualisation. The Income Tax Act exempts from capital gains in respect of transfer of capital assets from the non-corporate exchange to corporate exchange. Similarly, the Group on Demutualisation recommends that the brokers should hold shares in the exchange, should sit on the governing board of the exchange, and trade on the exchange. It is not different from the existing position. In fact, it recommends that the brokers, as such, should constitute one third of the governing board. The shareholders should also constitute one third of the board. It also says that the brokers can hold upto 50% of shares in the corporate exchange. This means that brokers, as shareholders, can constitute one sixth of the board and shareholders, who are not brokers, would constitute balance one sixth. Thus, the brokers would constitute 50% of the board, which is worse than the current situation. This is on the assumption that there are enough demand for equity holding in a demutual exchange. Otherwise brokers will have more than 50% equity and hence they would constitute majority in the board. The Group also does not object to continuation of membership card which not only combines all three rights, but also confers them on the same person. The focus should shift from corporatisation to demutualisation.

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