

BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No. 153 of 2008

Date of decision : 15.07.2009

Harinarayan G. Bajaj

..... Appellant

Versus

1. The Investors Protection Fund of Stock
Exchange, Mumbai

2. The Stock Exchange, Mumbai.

..... Respondents

Mr. Shailesh H. Bajaj, Constituted Attorney of the Appellant.

None for Respondent No.1.

Mr. P. N. Modi Advocate with Mr. Sagar Divekar Advocate for Respondent No.2.

Coram : Justice N.K. Sodhi, Presiding Officer
Samar Ray, Member

Per : Justice N.K. Sodhi, Presiding Officer

Harinarayan G. Bajaj is the appellant before us. He is an investor and trades, among others, on the Bombay Stock Exchange Limited, Mumbai (hereinafter called BSE) through several brokers. In this Appeal, we are concerned with only two brokers through whom the appellant had traded and they are Akhil K. Dalal and T. J. Stock Broking Services Private Limited (hereinafter called Dalal and TJ, respectively). The appellant has two arbitration awards in his favour. One of them is against Dalal and the other against TJ. The award against Dalal is for a sum of Rs.9,42,518.71 paise and against TJ for Rs.2,42,367.40 paise. These awards have become final between the parties and the appellant has been pursuing with BSE for the release of the awarded amounts without success. The appellant claims that the award against Dalal who has been declared a defaulter on the BSE should be paid out of the Investor Protection Fund which is a trust established by BSE for the protection and benefit of the constituents of defaulter members of the exchange. The amount due from TJ has also been withheld and BSE has invoked Bye-law 232(b) of its Bye-laws to justify the withholding. The claim of the appellant was finally rejected by BSE and its decision was communicated as per its letter dated October 29, 2003, the operative part of which reads as under:

“In view of the huge liabilities outstanding against you on the Exchange, the Board was of the opinion that an amount of Rs.9,42,518.71 towards the arbitration award obtained by you against defaulter Shri Akhil K. Dalal should not be paid from the IPF. On the same grounds the Board further decided that the payment of Rs.2,42,367.40 towards the arbitration award obtained by you against the member M/s. T.J. Stock Broking Ltd. from the assets of the member set aside by the Exchange should also not be released to you.”

It is against this communication that the present Appeal has been filed under section 23L of the Securities Contracts (Regulation) Act, 1956. For the sake of convenience, we shall deal with the grievance of the appellant in regard to the two awards separately.

Re - Award dated January 21, 2000 against Dalal:

2. The appellant traded in the scrip of Sesa Goa Limited through Dalal as his broker. Disputes arose between the two and the appellant claimed large sums of money in relation to his dealings with Dalal in this scrip from his broker. The dispute was referred to and decided by arbitration as per the Bye-laws of BSE since Dalal was a member broker of BSE. The Arbitral Tribunal of BSE by its award dated 21.1.2000 decided the reference in favour of the appellant and against Dalal and awarded in favour of the former a sum of Rs.9,42,518.71 paise with interest @ 18 per cent per annum on Rs.7,49,856/- from the date of reference till satisfaction and costs of the reference. As already noticed, this award has become final between the parties. The appellant claims that the awarded amount should be disbursed to him from the Investor Protection Fund maintained by the BSE as Dalal was a defaulter member broker of the exchange. It is not in dispute that Dalal was declared a defaulter on the BSE on 26.12.2000 and the default was notified on the exchange on 1.1.2001. As is clear from the impugned communication, the amount due to the appellant under the award has been withheld on the ground that he too owed large sums of money to others on the exchange. Whether this is a valid reason for withholding the amount is the sole question that arises for our consideration. Before we answer this question, it is necessary to go into the history as to how the Investor Protection Fund came to be set up and the manner in which it has thereafter evolved over a period of time.

3. Before the Securities and Exchange Board of India (hereinafter called the Board) came to be established in January 1992, the securities market in the country was being regulated directly by the Government of India. In the year 1985, the Government felt that there was no provision for payment of any dues to non-member clients (like the appellant herein) whenever a member broker is declared a defaulter on an exchange. In the light of the position which then existed, the Government felt that it was not conducive to instilling confidence in the minds of the investing public in the stock exchanges and felt that there was an imperative need for the creation of a compensation fund to take care of the legitimate investment claims which are not of a speculative nature of the clients of defaulting members. The Government then directed the stock exchanges across the country to set up a fund and limited the claims of each non-member to a maximum amount of Rs.10,000/- to begin with which could be raised progressively in the years to come. In pursuance to the directions of the Government of India, BSE established in the year 1986 a fund called “The Stock Exchange Customers’ Protection Fund” (hereinafter called the Fund) by creating a trust and got the same registered under the Bombay Public Trusts Act, 1950 and the rules framed thereunder. Trustees appointed by BSE manage the Fund. BSE has also framed the Stock Exchange Customers’ Protection Fund Rules (for short the Rules) which govern the fund. It is necessary to refer to clause 5A of the Trust Deed and Rule 7E of the Rules on which great reliance was placed by the learned counsel for BSE for justifying its action and they are reproduced hereunder for facility of reference:

“Clause 5A:-

The Trust shall be a Charitable Trust for the protection and benefit of the members of the public who invest and deal in securities through the members of the Stock Exchange. This Trust shall be compensating these members of the public in respect of their claims against defaulter members of the Stock Exchange in accordance with the provisions hereof and the Rules.”

“Rule 7E:-

Determination of nature of claims and payment:

The Trustees shall have an absolute discretion as regards the mode and method of assessing the nature of the claims including their genuineness and shall likewise at their discretion accept, reject, or partially grant or allow claims and make payment thereat subject to the limits hereinmentioned, as they may deem fit and proper.”

4. The Board was established on January 30, 1992 under the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as the Act) with a view to instill a sense of confidence in the public in the growth and stability of the capital market. Section 11 which is the summum bonum of the Act mandates that it shall be the duty of the Board to protect the interest of investors in securities and to promote the development of and to regulate the securities market by such measures as it thinks fit. The Board has been discharging this statutory duty by framing regulations, issuing guidelines, circulars and through other interventions, whenever necessary. Stock exchanges across the country including BSE are market intermediaries and subject to the regulatory control of the Board. The Board as a regulator does not interface directly with the investors and it is through the stock exchanges that the investor confidence is sought to be instilled in the public. During the course of inspection of the stock exchanges which is undertaken periodically, the Board observed that stock exchanges were following varying practices with respect to the setting up, management of and the disbursements from the Investor Protection Fund which they had maintained. With a view to bring about uniformity in the practices followed by stock exchanges with respect to the constitution, management and the utilization of proceeds of the fund, the Board issued on October 28, 2004 to all the stock exchanges in the country comprehensive guidelines on the Investor Protection Fund and the stock exchanges were advised to ensure that their Investor Protection Fund was in line with the provisions of the guidelines. The stock exchanges were required to take steps to make necessary amendments to their relevant bye-laws, rules and regulations for the implementation of the guidelines. The stock exchanges were further directed to bring to the notice of the member brokers/clearing members of the exchange, the provisions of the guidelines and they were also required to disseminate the same on their websites. The Board had further directed the stock exchanges to submit status report regarding the implementation of the guidelines. The circular issuing the guidelines made it clear that the same were being issued under section 11(1) of the Act to protect the interests of investors in securities and to promote the development of and to regulate the securities market.

5. We may now notice the salient features of the guidelines. Paras 1 to 4 deal with the constitution and management of the Investor Protection Fund which has to be administered by way of a trust created for the purpose. The trust has to consist of at least one public representative, one representative from the registered investors association recognised by the Board and the executive directors/managing directors/administrators of the stock exchange. The stock exchange has to provide the secretariat for the Fund which should be segregated and immune from any liability of the stock exchange. The guidelines further deal with the contributions to the Fund. They also provide for the manner in which claims are to be filed/invited from the investors by giving wide publicity through national newspapers as well as on the websites of the stock exchanges. The guidelines lay down benchmarks for determination of eligible claims and they recommend the adoption of arbitration mechanism at the stock exchange to determine the legitimacy of claims. The stock exchanges are free to fix suitable compensation limits for a single claim and it is common ground between the parties that BSE has by its notice no. 59522 of 2000 fixed the limit to Rs.10 lacs for each claim. Paras 21 to 24 of the guidelines deal with disbursements of claims from the Fund. They are relevant in the context of the present case and are reproduced hereunder for facility of reference:

- “21. The IPF/CPF Trust shall disburse the amount of compensation from the IPF/CPF to the investor and such a compensation shall not be more than the maximum amount filed for a single claim of an investor.
22. The IPF/CPF need not wait for the auction of the card of the defaulter member broker to realize the assets and the liabilities position of the defaulter member before the disbursements of the claims.
23. The IPF/CPF Trust shall disburse the compensation to the investors as and when claims have been crystallised against the defaulter.
24. The Stock Exchange shall ensure that the amount realized by the auction/close-out of the card realization of assets of the defaulter members are credited to the IPF/CPF after satisfying the claims of the Stock Exchange and the SEBI in accordance with the bye-laws of the Stock Exchange.”

Coming back to the facts of the present case, the claim of the appellant for disbursement of the amount awarded against Dalal from the Fund was first declined by the executive director of BSE on 7.12.2001. The claim was declined because BSE had received letters from two other brokers namely, SMK Shares and Stock Broking Pvt. Ltd. and

Shri Madhukar Sheth informing BSE that they had filed arbitration cases against the appellant for their claims against him. On receipt of these letters the executive director invoked Bye-law 232(b) of the Bye-laws and directed the trustees of the Fund not to pay the amount to the appellant. Feeling aggrieved by this order, the appellant filed Writ Petition no. 2520 of 2001 in the High Court at Bombay which was withdrawn on December 19, 2001 because BSE decided to reconsider the claim of the appellant and pass a fresh order. The trustees of the Fund in their meeting held on 14th March 2002 again considered the claim of the appellant and rejected the same on the ground that the arbitration proceedings were pending against the appellant and that the Board was then conducting investigations into the transactions of the appellant in Amara Raja Batteries.

The resolution passed by the trustees reads as under:

“RESOLVED that the application of Mr. Harinarayan Bajaj for the disbursal from the Investors’ Protection Fund of the amount of Rs.9,42,518.71 to Mr. Harinarayan Bajaj pursuant to the award dated 21st August, 1999 is hereby withheld and is made subject to the outcome of the pending arbitration reference against Mr. Harinarayan Bajaj as also the final decision of SEBI in its investigation of transactions of Mr. Harinarayan Bajaj in Amara Raja Batteries.”

The appellant again challenged the aforesaid decision of the trustees in Writ Petition no.1069 of 2002 in the High Court at Mumbai which was disposed off on October 19, 2002 with a direction that the appellant could prefer an appeal before the Governing Board of BSE under Rule 7(G) of the Rules. The appellant then filed an appeal before the Governing Board which was dismissed on January 27, 2003 on the ground that the amount could not be released from the Fund unless, in his turn, the appellant discharged his liabilities towards the payment of amounts due to M/s. Mahico Pvt. Ltd., another broker who had an arbitration award against the appellant. The Governing Board gave liberty to the appellant to file a fresh appeal after he discharges his crystalised liability towards M/s. Mahico Pvt. Ltd. Still not satisfied with the order of the Governing Board, the appellant filed Writ Petition no. 540 of 2003 before the High Court at Mumbai which was dismissed in limine on June 9, 2003. The learned Judges of the High Court referred to clause 5A of the Trust Deed and Rule 7E of the Rules framed by BSE and observed as under:

“5. Perusal of the aforesaid two provisions would show that the Trust may compensate the members of the public in respect of their claim against defaulter members of the Stock Exchange. The discretion to the Trust for determination of award of compensation is absolute and it may accept, reject or partially grant or allow claims and make payment to the concerned member of the public against defaulter member of the Stock Exchange. Such absolute discretion can also be exercised by withholding the amount payable to a member of the public against defaulting member of the Stock Exchange if the claimant is liable to pay some amount to some other persons of the claimant. In the facts and circumstances of the present case it cannot be said that an illegality was committed by the Stock Exchange Protection Fund in withholding the disbursement of the amount from the Investors Protection Fund in the sum of Rs.9,42,518.71 to the petitioner until the outcome of the pending arbitration references against the petitioner in Amara Raja Batteries.

6. No case for invocation of writ jurisdiction is made out.

7. Dismissed in limine.”

After the dismissal of the writ petition, the appellant paid up the amount due to M/s. Mahico Pvt. Ltd. and in terms of the liberty granted by the Governing Board of BSE, filed another appeal before it which was dismissed and the decision was communicated as per the impugned communication dated October 29, 2003, the relevant part of which has already been reproduced in the earlier part of our order. He again filed another Writ Petition no. 1460 of 2006 in the High Court challenging the communication dated October 29, 2003. This writ petition was admitted. Thereafter he moved a motion in the High Court and withdrew the writ petition on December 5, 2008 with liberty to file an appeal before this Tribunal. Hence this appeal.

6. It is in the light of the aforesaid guidelines that we have to examine the claim of the appellant that he should be paid the awarded amount from the Fund. Shri P.N. Modi, learned counsel for BSE referred to the Trust Deed dated July 10, 1986 by which the Fund was created and, particularly to clause 5A thereof and to Rule 7E of the Rules to contend that the exchange/board of trustees had an absolute discretion in the matter of disbursing amounts from the Fund and that they were justified in declining the claim of the appellant on the ground that there was a crystallized liability of about Rs.1.66 crore against him for which one Madhukar Sheth broker member has obtained an arbitration award against him. He relied upon the observations made by the learned Judges of the

High Court in Writ Petition no. 540 of 2003 and urged that the High Court had in clear terms laid down that the matter of disbursement from the Fund was in the sole discretion of the exchange/trustees and that BSE while declining the claim of the appellant had committed no illegality in the exercise of its discretion. He further contended that the order of the High Court dismissing the writ petition filed by the appellant operated as res judicata as he had raised the same plea before the Hon'ble High Court which was declined.

7. We have given our thoughtful consideration to the arguments advanced by Shri Modi and regret our inability to accept the same. It is true that the plea which the appellant is now raising before us had been raised before the Hon'ble High Court as well in Writ Petition no. 540 of 2003 which was rejected. As already noticed, the High Court had taken note of clause 5A of the Trust Deed and Rule 7E of the Rules and observed that the discretion conferred by these two provisions on the trustees in the matter of disbursement from the Fund was absolute and that BSE committed no illegality in withholding the amount payable to the appellant as he was liable to pay some amount to some other persons. The High Court had also taken note of the fact that proceedings against the appellant were pending in the case of M/s. Amara Raja Batteries Ltd. The High Court gave its decision on June 9, 2003 when there were no guidelines issued by the Board and the entire matter of disbursement was governed by the provisions of the Trust Deed and the Rules thereunder. After the High Court rendered its decision and rejected the claim of the appellant, the Board came out with comprehensive guidelines issued under section 11(1) of the Act dealing with the constitution, management and utilization of the Fund. These guidelines have a statutory force. As already noticed, the Board had directed all the stock exchanges to bring about necessary amendments in their respective trust deeds/rules/regulations governing such funds so as to bring their fund in line with the guidelines. Paras 21 to 24 of the guidelines have already been reproduced in the earlier part of the order which when read together with other relevant paragraphs of the guidelines take away the discretion from the exchange/board of trustees in the matter of disbursements from the Fund and

make it mandatory that all eligible claims shall be disbursed from the Investor Protection Fund. Paras 12 to 15 of the guidelines define the eligible claims. These paragraphs make it clear that the claim made by a client against a defaulting member of the exchange is an eligible claim and the only claims which could be rejected under the guidelines are those arising out of speculative transactions. A speculative transaction is one in which the contract for the purchase or sale of shares or debentures is settled otherwise than by actual delivery or transfer of the scrips. It is common ground between the parties that the claim of the appellant herein does not arise out of speculative transactions. The claim of the appellant being eligible under the guidelines has to be disbursed from the Fund as it does not exceed the maximum amount fixed by BSE for payment of compensation to the investors on account of default of members. This is the mandate of paragraphs 21 and 23 of the guidelines which have been reproduced earlier. Normally, when a broker member defaults on the exchange, his membership card was auctioned with a view to realize his assets and liabilities before disbursement claims were entertained. Para 22 of the guidelines brings about a change that the exchange/Investor Protection Fund need not wait for the realization of assets and liabilities and that the claim should be disbursed to the client. Para 23 further makes it clear that once a claim has been crystallized the trust shall disburse the same. The appellant is claiming the amount under an arbitration award which he has obtained against Dalal and having become final the claim has crystallized. We are of the view that the claim of the appellant satisfies all the requirements of the guidelines for disbursement from the Fund and that the amount cannot be withheld on the ground that another broker has a claim against him. It is clear that the claim of a broker against the appellant cannot be met from the Fund. If Madhukar Sheth a broker member of the exchange has an award against the appellant, he can enforce the same in accordance with law. On this ground, the claim of the appellant against Dalal which stands crystallized cannot be withheld.

8. When faced with this situation, Shri P. N. Modi, learned counsel for BSE contended that the trust deed of the Fund and the Rules have not been amended since

the publication of the guidelines and, therefore, the disbursement from the Fund shall continue to be governed by the trust deed and the Rules. He further contended that the Board has not insisted upon BSE to amend its trust deed or the rules so as to bring them in line with the guidelines. We cannot accept this argument. The guidelines which are statutory in force shall override the provisions of the trust deed and the Rules insofar as they are inconsistent with the provisions of the guidelines and it is the guidelines which shall govern disbursements from the Fund. The guidelines have taken away the absolute discretion which earlier vested in the Board of Trustees and the claims of the investors now have to be met strictly in accordance with the guidelines. The very purpose of issuing the guidelines was to make the stock exchanges across the country adopt a uniform pattern in the matter of constitution, management and utilization of the Fund. No exchange can defeat the claim of an investor, if it is otherwise eligible under the guidelines, merely because it failed to amend its trust deed or rules governing the Investor Protection Fund in accordance with the guidelines. It is high time BSE brought its trust deed and the Rules in accordance with the guidelines and realize that disbursements from the Fund are no longer in its absolute discretion. These will have to be governed by the guidelines. The High Court Order in W.P. 540 of 2003 does not operate as res judicata because it did not consider the guidelines which brought about a substantial change as these were issued long after its order. In this view of the matter, the action of BSE in withholding the amount due to the appellant from Dalal cannot be sustained.

Re - Award dated January 16, 2003 against TJ:

9. As already observed, TJ is a registered stock broker and the appellant has an arbitration award against it in a sum of Rs.2,42,367.40 paise. Madhukar Sheth is another broker on BSE and he has obtained an award against the appellant in a sum of Rs.1,65,97,149.57 paise. Madhukar Sheth informed BSE that he had a claim against the appellant and, therefore, the amounts due to the latter should not be disbursed. BSE invoked the provisions of Bye-law 232(b) of its Bye-laws and by the impugned communication dated October 29, 2003 informed the appellant that the amount due to him from TJ

had been set apart but was not being released to him. Clause (b) of Bye-law 232 of the Bye-laws of BSE provides that if a creditor member has a claim against a defaulting constituent, then the secretary of the exchange shall direct any member or members not to pay or deliver to the defaulting constituents any monies or securities upto an amount or value not exceeding the creditor member's claim payable or deliverable by him to the defaulting constituent. The appellant claims that the amount due to him under the award against TJ should be released to him under the interim orders passed by the Supreme Court in I.A. no. 3 of 2008 filed in Appeal no. D36176 of 2008. We find merit in this claim of the appellant as well. While the appellant was pursuing his claims with BSE for the disbursement of the amounts due to him under the awards against Dalal and TJ, the Board had initiated action against the appellant and his son under sections 11 and 11-B of the Act and by order dated June 25, 2003 directed the appellant and his son to disassociate themselves from the capital market for a period of 5 years and they were also prohibited from dealing in securities for a period of 10 years. Feeling aggrieved by this order, the appellant and his son both filed Appeal no. 117 of 2003 before this Tribunal which was allowed on 10.10.2007 and the order dated June 25, 2003 was set aside. The Board then filed Appeal no. D36176 of 2008 in the Hon'ble Supreme Court against the order of the Tribunal, which is pending. In the pending Appeal, the Board filed I.A. no. 3 of 2008 in which it made the following two prayers:

“It is, therefore, most respectfully prayed that this Hon'ble Court may be pleased to:

- (a) pass an order staying the operation of the Judgment and final order passed by the Securities Appellate Tribunal (SAT), Mumbai in Appeal No. 117 of 2003;
- (b) pass an order restraining the Respondents herein from receiving from the BSE the monies payable to them for their trading in Settlement no. 51/2001 of BSE as also any other amount(s) that may be payable to them by the BSE;”

Along with this I.A, the Board had attached a statement showing the details of the brokers through whom the appellant had traded and this list includes the name of TJ as well as Madhukar Sheth who has a claim against the appellant. On this I.A. their Lordships of the Supreme Court passed the following order on 7.4.2008:

“Hearing of the Civil Appeal stands expedited.

Pending the hearing and final disposal of the Civil Appeal, respondents herein would be entitled to receive from the brokers of Bombay Stock Exchange monies payable to them for trading, subject to the result of the Civil Appeal.

The I.A. is disposed of.”

It is thus clear that the prayer for stay made by the Board was not granted. A prayer made and not granted is deemed to have been rejected. Be that as it may, the learned Judges specifically directed that the respondent before them (the appellant herein) “would be entitled to receive from the brokers of Bombay Stock Exchange monies payable to them for trading, subject to the result of the Civil Appeal.” This order in no uncertain terms establishes the claim of the appellant to receive the amount due from the brokers of BSE including TJ notwithstanding Bye-law 232 (b) of its Bye-laws. Shri Modi appearing for BSE contended that it was not a party in the appeal before the Supreme Court and, therefore, it was not bound to comply with the order. It is true that BSE is not a party before the Supreme Court but it cannot be heard to say that it is not bound by the order. If it wants to continue to withhold the amount due to the appellant in the exercise of its power under Bye-laws 232 (b), it should have moved an application in the Supreme Court to get the order modified. Not having done so, it is bound to implement the order. In view of the interim order passed by the Supreme Court, the appellant is entitled to the release of the amount due to him from TJ which BSE has already set apart from its (TJ’s) margin money/security.

For the reasons recorded above, the appeal is allowed and the impugned communication dated October 29, 2003 by which BSE has withheld the amounts due to the appellant from Dalal and TJ set aside. BSE is directed to release forthwith the amounts under the two awards. There is no order as to costs.

After we pronounced the order, the learned counsel appearing for the respondents made an oral request to stay the operation of our order to enable the respondents to file an appeal in the Supreme Court. Having regard to the fact that the appellant has not received the amounts for the last almost ten years, we direct that our order shall come into operation after four weeks from today.

Sd/-
Justice N.K. Sodhi
Presiding Officer

Sd/-
Samar Ray
Member

15.07.2009
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Prepared & Compared by
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