

BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Date of Decision: 11.11.2014

Appeal No. 29 of 2014

Share India Securities Ltd.
(Formerly known as FMS Securities Ltd.)
14, Dayanand Vihar,
Near Karkardooma Metro Station,
Delhi- 110 092

...Appellant

Versus

Securities and Exchange Board of India,
SEBI Bhavan, Plot No. C-4A, G-Block,
Bandra-Kurla Complex, Bandra (East),
Mumbai - 400 051

...Respondent

Mr. Prakash Shah, Advocate for the Appellant.

Mr. Kumar Desai, Advocate with Mr. Mihir Mody, Advocate for the Respondent.

CORAM: Justice J.P. Devadhar, Presiding Officer
Jog Singh, Member
A.S. Lamba, Member

Per: Justice J.P. Devadhar (Oral)

1. Whether the Adjudicating Officer (“AO” for short) of Securities and Exchange Board of India (“SEBI” for short) is justified in imposing penalty of ₹ 5 lac under Section 15F and penalty of ₹ 5 lac under Section 15HB of the SEBI Act, 1992 (“SEBI Act” for short) on the appellant is the question raised in this appeal.

2. Facts relevant to the present appeal are that on receipt of complaints from various investors against Rishabh Shares and Securities (“Rishabh” for short) which was registered as a sub-broker of M.G. Capital Services Ltd. (“M.G. Capital” for short) on the National Stock Exchange (“NSE” for short), SEBI conducted investigation and inspected the books of account and other documents of Rishabh.

3. On examination of documents/information received from various entities it was noticed that Rishabh had traded on the Bombay Stock Exchange (“BSE” for short) as a constituent i.e. as a client of the appellant. Rishabh had maintained a running account with the appellant which was settled not by making payment into the bank account of Rishabh as required under SEBI circular dated August 27, 2003 but by making payment through M.G. Capital a sister concern of the appellant, with whom Rishabh had an account as a sub-broker of M.G. Capital. Since payment was made by appellant to Rishabh in violation of SEBI circular dated August 27, 2003, show cause notice was issued to the appellant. Similarly it was noticed, that contrary to the claim of the appellant that Rishabh had traded as a client of the appellant, Rishabh had in fact traded on BSE on behalf of its clients as a sub-broker of the appellant. Since appellant had allowed Rishabh to trade on behalf of its clients on the BSE without Rishabh being registered as sub-broker of appellant for trading on BSE, it was considered that appellant had violated regulation 18B of the Securities and Exchange Board of India (Stock Brokers and Sub-brokers) Regulations, 1992 (“Brokers

Regulations” for short) read with SEBI circular dated May 21, 2003 read with Clauses A(1),A(2) & A(5) of the Code of Conduct for Stock Brokers mentioned under schedule II of the Brokers Regulations read with regulation 7 of the Brokers Regulations. Accordingly, by the aforesaid show cause notice appellant was called upon to show cause as to why penalty should not be imposed for violating SEBI circular dated August 27, 2003 as also regulation 18B of Brokers Regulations.

4. Appellant filed reply to the show cause notice, wherein it was stated that appellant has not committed any violations. Personal hearing was also granted to the appellant. Thereafter, by the impugned order, penalty of ₹ 5 lac under Section 15F and penalty of ₹5 lac under Section 15HB of SEBI Act has been imposed upon the appellant. Challenging the aforesaid order present appeal is filed.

5. With reference to imposition of penalty of ₹ 5 lac under Section 15F(b) of SEBI Act, it is contended by Mr. Shah, learned counsel for the appellant that SEBI circular dated August 27, 2003 applies to the payments to be made by broker to the client. Since SEBI has held that Rishabh has traded through the appellant as a sub-broker and not as a client, it is not open to SEBI to hold that the appellant has violated SEBI circular dated August 27, 2003, because, the said circular relates to making payment by a broker to a client and not to a sub-broker. It is further contended that since stock exchange (NSE) permits utilization of free balance (funds/collaterals) of a client lying in the books of the trading member’s associate group entities, it cannot be said that the

appellant has violated SEBI circular dated August 27, 2003 by making payments to Rishabh through M.G. Capital.

6. We see no merit in the above contentions. As per SEBI circular dated August 27, 2003 it was mandatory for the appellant as a broker to make all payments to Rishabh who had traded as a client of the appellant, strictly by account payee cross cheques/demand drafts or by way of direct credit into the bank account through EFT, or any other mode allowed by SEBI. Having permitted Rishabh to trade on BSE as a client of the appellant, it was obligatory on part of appellant to make payment due to Rishabh in the manner specified under the said circular. As the payment was not made in the manner specified under that circular, it is apparent that the appellant has violated SEBI circular dated August 27, 2003.

7. Argument of the appellant that in view of the finding recorded by SEBI that Rishabh has traded through the appellant as a sub-broker, it cannot be said that the appellant has violated SEBI circular dated August 27, 2003 is without any merit because, firstly, as a matter of fact, Rishabh had traded through the appellant on the BSE by representing to be a client of the appellant and, in such a case, the appellant was obliged to make payment in the manner specified under SEBI circular dated August 27, 2003. Fact that on investigation SEBI has found that Rishabh instead of trading as a client, has traded on behalf of its clients as a sub-broker of appellant does not absolve appellant from its obligation to make payment in the manner specified under SEBI circular dated

August 27, 2003, especially when appellant claims to have permitted Rishabh to trade as a client of the appellant. Secondly, what is held in the impugned order is that Rishabh acted as a sub-broker without actually being registered as a sub-broker which was in violation of regulation 18B of Brokers Regulations. Thirdly, SEBI circular dated August 27, 2003 cannot be construed to mean that the said circular permits a broker to pay to a sub-broker, by a mode otherwise than the mode specified under SEBI circular dated August 27, 2013. Therefore, in the facts of present case, having permitted Rishabh to trade as client, appellant cannot escape penal liability for violating SEBI circular dated August 27, 2003, merely because SEBI on investigation found that the appellant in the guise of permitting Rishabh to trade as a client has in fact permitted Rishabh to trade on BSE on behalf of its clients as a sub-broker of the appellant. In this view of the matter, in our opinion, no fault can be found with the decision of SEBI in imposing penalty under Section 15F(b) of SEBI Act for violating SEBI circular dated August 27, 2003.

8. Quantum of penalty imposable under Section 15F(b) of SEBI Act is ₹ 1 lac for each day during which failure to make payment as per SEBI circular dated August 27, 2003 continues or ₹ 1 crore whichever is less. Since, payment has not been made in the manner specified under SEBI circular dated August 27, 2003 till date, the penalty imposable on appellant would be ₹ 1 crore. However, after considering all mitigating factors the AO has imposed penalty of ₹ 5 lac under Section 15F(b) of

SEBI Act which cannot be said to be unreasonable, arbitrary or excessive.

9. With reference to imposition of penalty of ₹ 5 lac under Section 15HB of SEBI Act, 1992 for allegedly violating regulation 18B of Brokers Regulations, counsel for the appellant submitted that in view of decision of Delhi High Court in the case of National Stock Exchange Member vs. Union of India reported in [2006] 70 SCL 151 (DELHI) it cannot be said that the appellant has violated regulation 18B of the Brokers Regulations. Submission is that, since Rishabh was registered as sub-broker of M. G. Capital for trading on NSE, there was no need for Rishabh to obtain another certificate for the purpose trading on BSE through the appellant.

10. Section 12(1) of SEBI Act which deals with registration certificate (to the extent relevant) reads as under:-

“12. Registration of stock-brokers, sub-brokers, share transfer agents, etc-(1) No stock-broker, sub-broker, share transfer agent, banker to an issue, trustee of trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and such other intermediary who may be associated with securities market shall buy, sell or deal in securities except under, and in accordance with, the conditions of a certificate of registration obtained from the Board in accordance with the [regulations] made under this Act.”

11. Construing aforesaid provisions contained in Section 12(1) of SEBI Act, Delhi High Court has held thus:-

“4. A bare perusal of section 12(1) makes it clear that only one certificate of registration from the

SEBI is required even if a stock broker operates from several stock exchanges in the country. In fact, section 12(1) does not refer to any stock exchange at all. All it states is that a stock broker can do business in buying or selling securities only after getting a certificate of registration from the SEBI in accordance with the regulations made under the Act. The expression 'certificate' means only one certificate."

12. Aforesaid decision of the Delhi High Court clearly supports the contention of the appellant. Counsel for SEBI, however, submitted that aforesaid decision of the Delhi High Court has been challenged before the Apex Court and while admitting the appeal, the Apex Court has directed the parties therein to maintain status quo till the disposal of the appeal and, hence, appellant is not justified in relying upon the decision of the Delhi High Court. It is further contended by counsel for SEBI that the decision of Delhi High Court is distinguishable, because, in the said decision neither the scope of regulation 11 of Brokers Regulations as it then stood nor Brokers Regulations 18B inserted with effect from September 23, 2003 has been considered and therefore reliance placed on the Delhi High Court decision is misplaced.

13. We see no merit in the above contentions raised by the counsel for SEBI. Section 12 of SEBI Act is the main Section which deals with registration certificate. PIT Regulations are framed in implementation of the provisions contained in the SEBI Act. Once Delhi High Court in the aforesaid case has construed Section 12 of SEBI Act and held that separate registration certificate is not necessary for trading in each stock exchange, it would not be proper to hold that regulation 11(as it then

stood)/12/18B of PIT Regulations contemplate separate registration certificate especially when the language used in all those regulations even remoted suggest that separate registration certificates are required to be obtained. Therefore, in the facts of present case, decision of SEBI in holding that the appellant is guilty of violating regulation 18B of Brokers Regulations cannot be sustained, because, admittedly the appellant had registration certificate for trading on NSE and as per Delhi High Court decision, appellant was not required to obtain separate registration certificate for trading on BSE.

14. It is relevant to note that after the aforesaid decision of the Delhi High Court, new regulation 11 has been inserted by the SEBI (Stock Brokers and Sub-brokers) (second amendment) Regulations 2006, w.e.f. September 7, 2006 where the language used is different from the language used in regulation 11 as it stood at the time relevant to the present appeal. In the present case, we are concerned with payments made prior to September 7, 2006, hence, new regulation 11 which came into force w.e.f. September 7, 2006 would not be relevant to the present case. Since the decision of the Delhi High Court is pending before the Apex Court, we do not express any opinion on the scope and ambit of Section 12 of SEBI. However, in view of Delhi High Court decision which holds the field as on date, in our opinion, decision of SEBI in holding that the appellant is guilty of violating regulation 18B of Brokers Regulations and accordingly imposing penalty of ₹ 5 lac on appellant is unjustified. Although, the Apex Court in the appeal filed

against the Delhi High Court decision has directed the parties therein to maintain status quo, the said direction would not apply to the facts of present case, because, the running account between the appellant and Rishabh has already been closed. Accordingly, penalty of ₹ 5 lac imposed under Section 15HB of SEBI Act shall stand deleted.

15. In the result, appeal is partly allowed by sustaining the penalty imposed under Section 15F(b) of SEBI Act and deleting the penalty of ₹ 5 lac imposed under Section 15HB of SEBI Act.

16. Appeal is disposed of in above terms with no order as to costs.

Sd/-
Justice J.P. Devadhar
Presiding Officer

Sd/-
Jog Singh
Member

Sd/-
A S Lamba
Member

11.11.2014
Prepared & Compared By: PK