

IN THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No. 53 of 2007

Date of decision : 10.12.2007

Mukesh Babu Securities Limited

..... Appellant

Versus

1. Securities and Exchange Board of India
2. Central Depository Services (India) Ltd.

.....
Respondents

Mr. N.H. Seervai Senior Advocate with Mr. S.H. Merchant, Ms. R.S. Merchant and Ms. Chaitra Rao Advocates for the Appellant.
Dr. Poornima Advani Advocate with Ms. Sejal Shah Advocates for the Respondent No.1
Mr. Devesh Juvekar Advocate for the Respondent No.2.

Coram : Justice N.K. Sodhi, Presiding Officer
Arun Bhargava, Member
Utpal Bhattacharya, Member

Per : Justice N.K. Sodhi, Presiding Officer

This order can conveniently dispose of four Appeals nos. 62 & 304 of 2004, 72 of 2006 and 53 of 2007 all of which have been filed by Mukesh Babu Securities Limited. For the view that we are taking in Appeal no. 53 of 2007 the other three appeals shall also have to be dismissed.

Appeal no. 53 of 2007

Mukesh Babu Securities Limited (for short the company) was incorporated in February 1994 as a private limited company which later became a public limited company. It is a member of the National Stock Exchange of India Ltd. (NSE) and also of the Bombay Stock Exchange Ltd. (BSE) and the Central Depository Services (India) Ltd. (CDSL) which is

thereunder and the Depositories Act, 1996. It has entered into an agreement with CDSL as its agent and is affiliated to it. The certificate of registration was granted by the Board in June, 1999 for a period of five years which was valid upto June 28, 2004. In January 2004 CDSL sent a communication to the company informing the latter that its registration was coming to an end in June 2004 and that the last date for application to be submitted to the Depository (CDSL) was February 18, 2004 and that the last date for forwarding that application to the Board for renewal of the certificate was 18th March, 2004. CDSL asked the company to file an application for the renewal of its registration as a participant. In response to the aforesaid letter, the company filed an application on 16.2.2004 in Form E seeking renewal of its registration as a participant and the same was sent to CDSL which was forwarded to the Board for granting renewal. After receipt of the application by the Board, it appears that it (Board) was prima facie of the view that the grant of registration to the company may not be in the interests of investors in the securities market. It also appeared to the Board prima facie that the company was not a fit and proper person as it did not conform to the requirements of Regulations 19(cc) and 19(d) of the Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996 (hereinafter referred to as 1996 Regulations). The Board was also of the view that it was in public interest to inquire into the affairs and dealings of the company to find out the possible violations of the 1996 Regulations. Inquiry proceedings under the Securities and Exchange Board of India (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (for short the enquiry regulations) were initiated presumably for cancelling the certificate of registration already granted and an enquiry officer was appointed. The

be imposed on an erring intermediary. A copy of the proceedings by which the enquiry officer had been appointed was annexed to the notice which stated that the company was not a fit and proper person and that it was not in the interests of investors in securities market to grant a certificate of registration. The Board also took up simultaneously the application of the company seeking renewal of its certificate of registration. It issued another notice to the company under Regulation 24(1) of the 1996 Regulations calling upon it to show cause why its application for renewal be not rejected for the following reasons as it was prima facie of the view that the company was not a fit and proper person in terms of Regulation 19(cc) of the 1996 Regulations read with Regulations 3(2)(f) & 3(2)(h) of the Securities and Exchange Board of India (Criteria for Fit and Proper Person) Regulations, 2004 (for short Fit and Proper Person Regulations):

- “1. Your alleged involvement in Madhavpura Mercantile Co-operative Bank Limited case.
2. The order dated February 12, 2004 passed by SEBI rejecting your application for renewal of registration as a Depository Participant of NSDL.
3. CDSL has not recommended the application for renewal. CDSL has requested SEBI to take a view in this regard.
4. Order of warning was issued against you by SEBI in the Amar Raja Batteries case.
5. An inquiry has been initiated against you in the case of Global Trust Bank Limited.
6. An enquiry has been initiated against you in the case of Ranbaxy Laboratories Limited.”

Regulation 24(1) provides that if the Board is to reject an application for renewal it shall do so after giving the applicant an opportunity of being heard.

Mercantile Co-operative Bank Limited (for short the Bank) and also for the reason that by order dated February 12, 2004 the Board had rejected its application for renewal of registration as a participant of the National Securities Depository Limited (NSDL). He observed in his report that Shri. Mukesh Babu chairman of the company had been arrested by the Central Bureau of Investigation (CBI) in connection with the Madhavpura Bank scam for his alleged involvement therein which had a bearing on the capital market and, therefore, the company was not a fit and proper person to continue as a participant of CDSL. He, accordingly, recommended cancellation of the certificate of registration of the company as a participant of CDSL. On receipt of the enquiry report, the Board issued another notice dated 3.5.2006 to the company to show cause why the report be not accepted and its certificate of registration not cancelled. A copy of the report was sent alongwith the notice. The company filed a detailed reply dated 19.5.2006 stating that it was a fit and proper person and that the order dated February 12, 2004 by which its application for renewal of its certificate of registration as a participant of NSDL had been rejected had been challenged before this Tribunal in Appeal no.62 of 2004 which was then pending. It is pertinent to mention that Appeal no. 62 of 2004 is being disposed of alongwith this appeal.

The whole time member of the Board took up for consideration in the year 2006 the enquiry report submitted by the enquiry officer along with the reply filed by the company. He also took up alongwith it the application of the company seeking renewal of the certificate of registration. This application though pending since March 2004 had been kept on hold pending enquiry. The Board took note of the fact that Shri. Mukesh Babu the chairman of the company had been taken into custody by the CBI and was later released on

CBI. The CBI has filed the charge-sheet in the court of Chief Metropolitan Magistrate, Ahmedabad in which Mukesh Babu, among others, has been shown as an accused. In view of the pendency of this criminal case in which serious charges have been levelled against all the accused including Mukesh Babu, it came to the conclusion that the company was not a fit and proper person within the meaning of Regulations 3(2)(f) and 3(2)(h) of the Fit and Proper Person Regulations. Since the certificate of registration already granted to the company in June 1999 had by then expired, the question of cancelling the same did not arise and, therefore, the Board passed no order in the enquiry proceedings. The Board, however, by its order dated 19.1.2007 rejected the application of the company seeking renewal of its certificate of registration as a participant of CDSL. It is against this order that the present appeal has been filed under section 15T of the Act.

We have heard Shri. N.H. Seervai learned senior counsel on behalf of the appellant and Dr. Poornima Advani Advocate on behalf of the Board and they have taken us through the record of the case. We have also gone through the impugned order and it is clear therefrom that the company has been held not to be a 'fit and proper person' in terms of Regulations 3(2)(f) and 3(2)(h) of the Fit and Proper Person Regulations because Mukesh Babu, its chairman is shown as an accused in a criminal case which is pending in the court of Chief Metropolitan Magistrate, Ahmedabad. The substantive offence with which he has been charged is under section 420 IPC read with sections 409 and 120-B IPC.

At this stage, it would be relevant to refer to the criminal case that is pending in the court of Chief Metropolitan Magistrate, Ahmedabad. On a complaint filed by the Administrator of the Bank appointed by the Reserve

only against S/Shri. Rameshchandra Parikh, Devendra Pandya and Jagdish Pandya. Shri. Rameshchandra Parikh was the chairman of the Bank, Shri. Devendra Pandya was its managing director and Jagdish Pandya was the manager of the Mandvi branch of the Bank at Mumbai. By order dated 2.5.2001 passed by the Hon'ble High Court of Gujarat the investigation of the case was transferred to the Central Bureau of Investigation, Bank Securities & Fraud Cell, Mumbai. The case was registered by the CBI on 18.5.2001. After investigations were completed the CBI filed the charge-sheet in the court of Chief Metropolitan Magistrate, Ahmedabad some time in the year 2003 arraying as many as 11 accused therein including Shri. Mukesh Babu-the chairman of the company. CBI has commented on the role of Mukesh Babu and his four companies through which he had overdrawn the money and this is what it has to say in para 12 of the charge-sheet :

“12. That, the total unlawful loss suffered by the MMCB was 1029.15 crore, of which loss of Rs.778.57 crore was through the accounts of Sh. Ketan Parekh (A-4); Rs.206 crore was through the accounts of Sh. Mukesh Babu (A-6); Rs.19.32 crore was through the accounts of Sh. Shirish Maniar (A-7); Rs.19.86 crore was through the account of M/s. Triumph International, belonging to S/Sh. Dharmesh Doshi (A-8) and Jatin Sarvaiya (A-9) and Rs.5.40 crore was through the account of M/s. Prithvi Marketing.”

Again in para 17 of the charge-sheet reference has been made to the role of Shri. Mukesh Babu in the following words:

“17. That, the Rs.206 crore overdrawn through the accounts of Sh. Mukesh Babu (A-6) had also gone to make good the losses suffered on account of speculative trading and out of Rs.206 crore, Rs.98 crore was on account of trading loss incurred by Sh. Rameshchandra Parikh (A-1), who did the trading through a terminal extended by Sh. Mukesh Babu (A-6). This clearly establishes the criminal conspiracy and overt criminal acts. In pursuance of the conspiracy, another Rs.25 crore was transferred from the account of Sh. Mukesh Babu (A-6) to the account of M/s. Madhur Capital & Finance of A-

include Shri. Mukesh Babu. It is further stated that in pursuance to the said criminal conspiracy they have committed various illegal acts which resulted in wrongful loss to the depositors of the Bank and corresponding wrongful gain to the accused. The CBI has then assigned specific roles to each of the accused and this is what it has to say qua Mukesh Babu in sub-para (vi) of para 21:

“21...Their specific roles in the said criminal conspiracy are as follows:

(i).....

(ii).....

(iii).....

(iv)

(v).....

(vi) Sh. Mukesh Babu (A-6) is the Managing Director of 5 borrowal accounts, Cheques were signed and issued by him to cover the losses suffered by speculative share transactions done by Sh. Rameshchandra Parikh or by himself. Hence, his accounts ran an outstanding of Rs.198 crore. He is being Charged for offences punishable U/Sec. 120-B IPC r/w 409, 420 IPC Substantive offence U/Sec.420 IPC.”

We may now refer to the relevant Regulations on which reliance has been placed by the Board in the impugned order to hold that the company is not a fit and proper person. The relevant regulations read as under :

“Criteria for determining a ‘fit and proper person’

3.(1)”For the purpose of determining as to whether an applicant or the intermediary seeking registration under any one or more of the relevant regulations is a ‘fit and proper person’, the Board may take account of any consideration as it deems fit, including but not limited to the following criteria –

- (a) financial integrity;
- (b) absence of convictions or civil liabilities;
- (c) competence;
- (d) good reputation and character;
- (e) efficiency and honesty; and
- (f) absence of any disqualification to act as an intermediary as stipulated in these regulations.

(2) A person shall not be considered as a “fit and proper person” for the purpose of grant or renewal of certificate to act as an

(e).....

(f) an order withdrawing or refusing to grant any license/approval to the applicant or the intermediary, or its whole time director or managing partner which has a bearing on the capital market, has been passed by the Board or any other regulatory authority and a period of three years from the date of the order has not elapsed:

Provided that the Board may for reasons to be recorded in writing, allow the applicant or the intermediary, to seek registration before the lapse of three years as specified in clauses (d), (e) and (f).

(g).....

(h) any other reason, to be recorded in writing by the Board, which in the opinion of the Board, renders such applicant or the intermediary, or its whole time director or managing partner unfit to operate in the capital market.

Consideration of application for grant of certificate of registration.

19. For the purpose of grant of certificate of registration, the Board shall take into account all matters which are relevant to or relating to the efficient and orderly functioning of a participant and in particular, whether the applicant complies with the following requirements, namely :-

(a).....

(b).....

(c).....

(cc) the applicant is a fit and proper person; and

(d) the grant of certificate of registration is in the interests of investors in the securities market.”

The learned senior counsel for the appellant strenuously urged that the company cannot be said to be unfit to operate in the capital market merely because a criminal case has been registered against its chairman. He contended that what is stated in the charge-sheet filed by the CBI are only allegations which have yet to be proved in a court of law on the strict standards of proof required to establish a criminal charge. According to the learned senior counsel, the charge-sheet does not spell out clearly the role of Mukesh Babu and in any case the offence of cheating is not made out from the allegations made in the charge-sheet. The learned counsel for the respondent, on the other hand, strenuously argued that the criteria for ‘fit and proper

not take the risk of allowing the company to operate as an intermediary in the securities market as that may jeopardize the interests of the investors.

From the rival contentions of the parties and on a perusal of the impugned order, the short question that arises for our consideration is whether in the aforesaid factual background, the Board has erred in holding that the company is not a 'fit and proper person' to operate in the capital market.

As already noticed, a criminal case was registered against the chairman, managing director and manager of the Bank and they are alleged to have given overdraft facilities to several entities including the company by flouting all norms laid down by the Reserve Bank of India. Shri. Mukesh Babu- the chairman and managing director of the company is alleged to have had five borrowal accounts in the name of different entities including the company and after taking a loan facility of more than Rs.200 crores, he is said to have paid Rs.98 crores to make good the losses suffered by Shri. Rameshchandra Parikh- the chairman of the Bank who incurred these losses in speculative trading which was done through the terminals of the company. It is not in dispute that the company is also a stock broker registered with the Board and its certificate of registration was suspended due to some alleged market manipulations. That order is also under challenge in Appeal no.304 of 2004 which is being disposed of today. Shri. Mukesh Babu may not be responsible for the irregularities which the chairman and the managing director of the Bank might have committed in granting overdraft facilities but surely he was a beneficiary of those irregularities. Further, he paid Rs.98 crores to settle the speculative losses suffered by the chairman of the Bank. This is prima facie evidence of an unholy alliance. Apart from making a bald denial of its liability, the company has pleaded that the criminal case pending before the Chief Metropolitan

taken any overdraft facility nor has it denied that it paid Rs.98 crores to wipe out the losses suffered by the chairman of the Bank while trading through the terminals of the company. It is true that these are only allegations made in the charge-sheet and we are conscious that these are yet to be established in a court of law but from what is stated in the charge-sheet liaison between Shri. Mukesh Babu and the chairman of the Bank prima facie appears to be established. The CBI has alleged that there was criminal conspiracy among all the accused and that they have committed illegal acts which have resulted in wrongful loss to the depositors of the Bank and corresponding gain to the accused. The charges levelled are indeed serious and if established, they involve moral turpitude. We are unable to agree with the learned counsel for the appellant that the criminal case pending against Shri. Mukesh Babu and others has no concern with the securities market. It is through the terminals of the company that the chairman of the Bank had traded and incurred losses through speculative trading which losses have been made up by overdrawing money from the Bank. In these circumstances, the Board was entitled to take the view that the company was not a fit and proper person. It could not be said that Shri. Mukesh Babu or the company enjoyed good reputation within the meaning of the Fit and Proper Person Regulations. It has to be remembered that every intermediary of the securities market and every other person who associates himself with it has to satisfy the criteria for 'fit and proper person' as set out in Regulation 3 of the Fit and Proper Person Regulations and that it is mandatory for all registrants to adhere to those criteria through out the period of validity of their registration. When we look at the criteria in Regulation 3 it is clear that every applicant seeking fresh registration or seeking renewal of its registration has to possess financial integrity and should

across a large number of entities which may associate themselves with the market in one way or the other and which are governed by a host of regulations referred to in the schedule. If they are not fit and proper persons they cannot be allowed to access the securities market. An identical issue came up for consideration before this Tribunal in Jermyn Capital LLC vs. Securities & Exchange Board of India Appeal no. 21 of 2006 decided on 6.9.2006 wherein it was observed as under :

“A reading of the aforesaid provisions of the Regulations makes it abundantly clear that the concept of a fit and proper person has a very wide amplitude as the name “fit and proper person” itself suggests. The Board can take into account **“any consideration as it deems fit”** for the purpose of determining whether an applicant or an intermediary seeking registration

is a fit and proper person or not. The framers of the Regulations have consciously given such wide powers because of their concern to keep the market clean and free from undesirable elements. It can take into account the financial integrity of the applicant and its competence. Absence of convictions or civil liabilities would be another relevant consideration which could weigh with the Board. Good reputation and character of the applicant is a very material consideration which must necessarily weigh in the mind of the Board in this regard. Reputation is what others perceive of you. In other words, it is the subjective opinion or impression of others about a person and that, according to the Regulations, has to be good. This impression or opinion is generally formed on the basis of the association he has with others and/or on the basis of his past conduct. A person is known by the company he keeps. In the very nature of things, there cannot be any direct evidence in regard to the reputation of a person whether he be an individual or a body corporate. In the case of a body corporate or a firm, the reputation of its whole time director(s) or managing partner(s) would come into focus. The Board as a regulator has been assigned a statutory duty to protect the integrity of the securities market and also interest of investors in securities apart from promoting the development of and regulating the market by such measures as it may think fit. It is in the discharge of this statutory obligation that the Board has framed the Regulations with a view to keep the market place safe for the investors to invest by keeping the undesirable elements out. The Regulations apply across to all sets of regulations and all intermediaries of the securities market including those who associate themselves with the market and they all have to satisfy the criteria of “fit and proper person” before they could be registered under any of the relevant regulations and this criteria they must continue to satisfy through out the period of validity of their registration and

market rather than running the risk of allowing the market to be polluted. We may hasten to add here that when the Board decides to debar an entity from accessing the capital market on the ground that he/it is not a fit and proper person it must have some reasonable basis for saying so. The Board cannot give the entity a bad name and debar it. When such an action of the Board is brought to challenge, it (the Board) will have to show the material on the basis of which it concluded that the entity concerned was not a fit and proper person or that it did not enjoy a good reputation in the securities market. The basis of the action will have to be judged from the point of view of a reasonable and prudent man. In other words, the test would be what a prudent man concerned with the securities market thinks of the entity.....”

Applying the aforesaid tests, we are of the opinion that in the facts and circumstances of the case, the Board has taken a possible view which cannot be said to be perverse. It is not contrary to the material on record and nothing relevant has been ignored nor any irrelevant material taken into consideration. Thus, neither the decision nor the process followed by the Board suffers from any legal infirmity. In our opinion, the Board was justified in keeping the company out of the market as a risk containment measure in order to maintain its integrity and in the interests of investors. In view of the aforesaid, we answer the question posed in the earlier part of the order in the negative and hold that the Board has not erred in holding that the company is not a ‘fit and proper person’. Resultantly, the impugned order does not call for any interference by us in this appeal.

Appeal no. 62 of 2004

This appeal is directed against the order dated 12.2.2004 passed by the Board rejecting the application of the company for renewal of its registration as a participant of the National Securities Depository Limited on the ground that it would not be in the interests of investors in securities market to grant renewal. Reliance has been placed on Regulation 19 (d) of the 1996

Appeal no.72 of 2006

Challenge in this appeal is to the communication dated January 25, 2006 sent by the NSE to the appellant informing the latter that its trading facility on the Exchange would remain disabled since the criminal case pending in the Court of Chief Metropolitan Magistrate, Ahmedabad has still not been decided. We have already affirmed the order of the Board holding that the company is not a fit and proper person on that account and, therefore, it cannot be allowed to trade on the NSE. The impugned communication is, therefore, upheld.

Appeal no. 304 of 2004

In this appeal the company impugns the order dated September 10, 2004 passed by the Board suspending the certificate of registration of the appellant as a stock broker for a period of one year on the ground that it had entered into several synchronized transactions which were fictitious and not intended to transfer the beneficial ownership in the scrip of Global Trust Bank Limited. Even though the operation of the impugned order had been stayed during the pendency of the appeal, it is not necessary for us to examine the merits of that order in view of our findings recorded in Appeal no. 53 of 2007 that the company is not a fit and proper person. In view of our findings, this appeal has become infructuous.

In the result, all the four appeals are dismissed leaving the parties to bear their own costs.

Sd/-
Justice N.K. Sodhi
Presiding Officer