

BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Order Reserved on: 09.05.2019

Date of Decision : 10.06.2019

Appeal No. 285 of 2018

GRD Securities Limited
238A, A J C Bose Road,
6th Floor,
Kolkata – 700 012.

...Appellant

Versus

1. National Stock Exchange of India Limited
Exchange Plaza, Bandra Kurla Complex,
Bandra (E),
Mumbai – 400 051.

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

...Respondents

Mr. P.N. Modi, Senior Advocate with Ms. Kalpana Desai,
Advocate i/b Farooqui Mohammed Khalid, Advocate for the
Appellant.

Mr. Rashid Boatwalla, Advocate i/b Manilal Kher Ambalal & Co.
for Respondent No. 1.

Mr. Abhiraj Arora, Advocate with Mr. Vivek Shah, Advocate i/b
ELP for Respondent No. 2

CORAM : Justice Tarun Agarwala, Presiding Officer
Dr. C.K.G. Nair, Member
Justice M.T. Joshi, Judicial Member

Per : Dr. C.K.G. Nair, Member

1. This appeal is filed challenging the decision of the Disciplinary Action Committee ('DAC' for short) of the National Stock Exchange of India Limited ('NSE' for short) dated July 20, 2018 whereby the review application of the appellant was rejected. Consequently, the earlier decision of the DAC dated February 8, 2018 which directed the appellant to pay a penalty of Rs. 2,05,43,900/- and face suspension of one trading day in the currency derivative segment of the Exchange stood confirmed.

2. The appellant is a member broker in the Capital Market (CM), Futures and Options (F&O) and Currency Derivatives (CD) segments of the NSE. During a regular inspection of the books and records of the appellant for the calendar year 2016 in February 2017 NSE noticed that the appellant falsely reported margin amounting to Rs. 2,05,43,947/- in the CD segment in respect of two clients on two occasions on April 26, 2016 and June 21, 2016. Accordingly, DAC in its meeting held on January 12, 2018, after considering the oral and written submissions of the appellant, imposed a monetary penalty to the tune of Rs. 2,05,43,900/- and suspension of one trading day in the CD

segment after giving three weeks' notice. This was communicated to the appellant on February 8, 2018. This matter came up in appeal before this Tribunal which quashed the said order passed by the DAC of NSE on March 1, 2018 and directed the appellant to file a review application before the DAC. The order impugned in this appeal is issued by the DAC of NSE further to giving another opportunity of personal hearing to the appellant and considering their written submissions.

3. Shri P.N. Modi, the learned senior counsel for the appellant submitted that the alleged violations relate to delayed crediting of margin money collected from the clients. It is a technical mistake happened due to factors beyond the control of the appellant. For instance, in the case of the first alleged violation in respect of client Monotype India Ltd. the client had given cheques for Rupees One crore before trading on June 21, 2016. However, on account of a death in their family, on June 22, 2016 this client requested not to deposit the cheque for sometime, which is on record. Since the price moved in the expected direction there was no margin required on T + 5th day and hence no false reporting in the matter.

4. In the case of the second client as well cheques worth Rs. 65 lakh and 70 lakh were given by the client Viswakarma Metalicks Pvt. Ltd.. There was an inadvertent delay in depositing the cheques. However, the cheque was deposited on the T + 5 day and the same was cleared on the next day i.e. one day later. So it was again a technical error. It was also submitted that on account of these technical faults of the appellant no settlement issues happened nor the market was affected in any way.

5. It was further contended by the learned senior counsel for the appellant that though based on these factors this Tribunal had remanded the matter to DAC for reconsideration, the DAC did not apply its mind and has taken shelter behind SEBI circular dated August 10, 2011 and held that in view of the said circular the DAC has no discretion available with it in the matter once violation is established. The learned senior counsel contended that this stand is contrary to the Rules of the respondent NSE, particularly Rule 17 which states as follows:-

“Reconsideration / Review

(17) Subject to the provisions of the Securities Contracts (Regulation) Rules, 1957 the relevant authority may of its own motion or on appeal by the trading member concerned within 90 days from the date

of communication of decision of the relevant authority to the member reconsider and may rescind, revoke or modify its resolution withdrawing all or any of the membership rights or fining, censuring or warning any trading member. In a like manner the relevant authority may rescind, revoke or modify its resolution expelling or suspending any trading member.”

6. It was further submitted by the learned senior counsel that the appellant has been a broker for a long time and there has been no prior violation since 2011, nor any further violation during the year 2017, is found. Moreover, the brokerage earned by the appellant in the CD segment during the financial year 2016-17 was only about Rs. 3.1 lakh and the penalty imposed is more than Rs. 2.05 crore which is not only extremely harsh and disproportionate but if the appellant is obligated to pay such an amount there is no option other than closing down the business since such a hefty amount of penalty is beyond the reach of the appellant. In view of this the appellant sought to quash the impugned order treating it as a merely technical violation or alternatively reduce the amount of penalty to a modest sum.

7. Shri Rashid Boatwalla, learned counsel for the respondent no. 1 NSE, on the other hand, submitted that as per circular of SEBI dated August 10, 2011 the respondent NSE has no discretion which has been stated upfront in the impugned order by

the DAC. The said circular has been issued by SEBI to all Stock Exchanges after consultation with the Stock Exchanges which, inter alia, states as follows:-

“If during inspection it is found that a member has reported falsely the margin collection from clients, the member shall be penalized 100% of the falsely reported amount along with the suspension of trading for one day in that segment.

This circular is issued in exercise of powers conferred under Section 11(1) of the Securities and Exchange Board of India Act, 1992 read with Section 10 of the Securities Contracts (Regulation) Act, 1956 to protect the interests of investors in securities and to promote the development of, and to regulate the securities market.”

8. It was further submitted by the learned counsel for the respondent NSE that the appellant has given different reasons for the same delayed collection of margin in respect of the client Viswakarma Metalicks Pvt. Ltd. For instance, in their communication dated June 12, 2017 it was submitted that cheques of Rs. 65 lakh and Rs. 70 lakh were ‘unfortunately misplaced from the office premises.’ Vide letter dated January 12, 2018 it was stated that the cheque of Rs. 70 lakh was ‘unsigned’ as the client was travelling and cheque of Rs. 65 lakh was cleared one day late ‘due to late deposit in the bank.’ Further, vide letter dated March 15, 2018 it was stated that cheque of Rs. 70 lakh was

deposited on T + 11th day 'due to issue with signature.' These inconsistent statements from the side of the appellant reduced the veracity of the submissions.

9. Since this Tribunal noted that irrespective of the amount of margin involved or the number of instances of violations involved, the SEBI circular dated August 10, 2011 directs imposition of 100% of the falsely reported margin as penalty along with suspension of one day trading, on the direction of this Tribunal SEBI was also impleaded as Respondent No. 2, in order to ascertain the stand of SEBI on this matter. SEBI vide affidavit dated October 31, 2018 reiterated their stand as in the circular. In addition SEBI submitted that as per the communication dated October 4, 2018 of NSE, suspension of a trading member is not initiated if the instance of false reporting is less than 5% of the margin required to be collected and value of false reporting is less than Rs. 5 lakh. Since the present matter does not meet these criteria penalty of 100% margin and one day suspension imposed on the appellant is as per law.

10. We do not agree with the contentions of the appellant that it was only a technical violation. It is quite evident from the facts that though cheques may have been received from the clients the

appellant had not credited these amounts to the account upfront which is a basic requirement of margin collection from clients. Moreover in respect of client Monotype India it is not even clear whether the margin was ever collected. The submission that margin requirement as on T + 5, not as on the trading day, is what is relevant is not correct and hence not admissible. Upfront collection of margin is an important mechanism for ensuring prompt settlement and in promoting market integrity. As such any explanation to the contrary is not sustainable.

11. However, we are not able to agree with the stand of SEBI and NSE that no discretion in imposition penalty can be exercised, once a violation is established. The Circular issued by SEBI dated August 10, 2011 specifies different percentages of penalty with respect to short-collection / non-collection of margins from clients in equity and currency derivatives segment. While it specifies small proportion of 5% to 10% of margin short fall as penalty for non-reporting, it specifies that 100% of the short-collection shall be imposed as penalty. If such violation is noticed at the time of inspection then in addition to 100% penalty one day suspension has to be imposed. The said circular does not differentiate between situations involving upfront collection of cheques but late depositing or late crediting of the said amount and no upfront

collection at all and hence suffers from the proportionality principle. In order to incorporate proportionality, as is provided for small percentages of short falls in margin collection in the same circular itself, the word 'shall' in the circular has to be read as 'may' as it would enable the Exchange authorities to distinguish between no collection of margin at all and delayed collection of margin, particularly, in situations like no impact on the settlement or market at all. Accordingly, we are unable to agree with the interpretation of the spirit of the circular provided by SEBI as well as NSE. First of all Rule 17 of the NSE Rules quoted in paragraph 5 of this order clearly states that "the relevant authority has the power to reconsider and may rescind, revoke or modify its resolution withdrawing all or any of the membership rights or fining, censuring or warning any trading member. In a like manner the relevant authority may rescind, revoke or modify its resolution expelling or suspending any trading member. The relevant authority may modify its resolution expelling or suspending any trading member." These Rules are made under the Securities Contracts (Regulations) Act, 1956 (SCRA) and the SEBI Circular dated August 10, 2011 is issued under both SEBI Act and SCRA. Further, proportionality is a basic principle to be adhered to while interpreting any provisions relating to

punishment where the consequences are serious. In the instant case the violation is not in collecting the margin per se from the clients upfront but in delayed crediting of margin money. Delayed crediting of margin and not collecting the margin are not the same and has different consequences and cannot be treated on par. It is not in dispute here that the margin had been received by the appellant in the form of cheques; delay happened only in crediting the said amount to the account. This is quite different from not collecting the margin at all. It cannot be the intention of the law to treat both these situations identical when it comes to imposing a penalty. Penal consequences have to follow proportionality. It is also a matter of record that due to delayed collection no further consequences like a settlement failure has happened though it can be argued that post-events cannot be a ground as violation itself, irrespective of what happens thereafter, is the ground for imposing penalty. Though this argument is correct one cannot be totally oblivious to the post-event scenario from a proportionality angle. Therefore a violation which leads to a complete failure of the market or market integrity and a violation which has no impact on the market need to be distinguished in interpreting proportionality.

12. In this matter before us the penalty imposed is Rs. 2,05,43,900/- and suspension from trading in the Currency

Derivatives segment for one day. The appellant before us submits that the annual income from brokerage from CD segment is only to the tune of about Rupees three lakh which is not disputed. While we totally agree that upfront collection of margin is an important regulatory tool to safeguard market integrity, at the same time we are equally concerned with proportionality while imposing a penalty of a very heavy amount which can completely ruin an entity for a single violation. It is an undisputed fact that the appellant has not committed any other violation. While the SEBI circular is quite mechanical in directing the Exchanges to impose a fixed penalty, the Exchange Rules provide for an appeal / review and empowers the authority to review / rescind / reconsider the penalty imposed. Given these factors we are of the considered view that based on the facts and circumstances of the present matter, the law has to be interpreted in its spirit invoking proportionality.

13. Though we are inclined to reduce the penalty given these facts, the penalty has to be in tune with the violation. The appellant's submission that brokerage from the CD segment is only just over Rs. 3 lakh is incomplete since it has not disclosed the total earnings including that from other segments of the market. Moreover, it is imperative to underscore the importance of

prompt upfront margin collection for promoting market integrity. Balancing all these, a penalty of Rupees Fifty Lakh and one day suspension from the CD segment would meet the ends of justice in the matter. Appellant is directed to pay the penalty within four weeks from today. Respondent NSE shall implement the one day suspension after giving fifteen days notice to the appellant.

14. Appeal is partly allowed on the above lines. No order on costs.

Sd/-
Justice Tarun Agarwala
Presiding Officer

Sd/-
Dr. C.K.G. Nair
Member

Sd/-
Justice M.T. Joshi
Judicial Member

10.06.2019

Prepared and compared by:msb