BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Order Reserved on:17.9.2020
Date of Decision: 7.1.2021

Appeal No.210 of 2020

Edelweiss Broking Limited
Edelweiss House, Off. C.S.T. Road,
Kalina, Mumbai – 400 098. ... Appellant

Versus

National Stock Exchange of India Limited
Exchange Plaza, C-1 Block G,
Bandra Kurla Complex, Bandra (E),
Mumbai-400 051. …Respondent

Mr. Somasekhar Sundaresan, Advocate with Mr. Sameer Pandit, Ms. Krina Gandhi, Advocates i/b. Wadia Ghandy & Co. and Ms. Kamala Kantharaj, Authorised Representative for the Appellant.

Mr. Venkatesh Dhond, Senior Advocate with Mr. S. Vivek, Mr. Aditya Sikka, Ms. Drishti Das and Mr. Siddhant Sattur, Advocates i/b. Cyril Amarchand Mangaldas for the Respondent.

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

Per : Justice M.T. Joshi, Judicial Member

1. Aggrieved by the direction of the Member and Core Settlement Guarantee Fund Committee (hereinafter referred to as the 'Committee') of the respondent National Stock Exchange of India Limited to pay a penalty of Rs.1,80,10,000 on account of two violations vide order dated 6th June, 2020 the appellant has preferred the present appeal.

2. The appellant is a member registered with the exchange in the capital market and futures and options segment. Inspection of the record of the appellant was carried out for the period from April 1, 2017 to February 28, 2019. As certain violations were noted appropriate disciplinary action was started by the Committee in view of the joint Committee meeting decision with Securities and Exchange Board of India (hereinafter referred to as 'SEBI') . Show cause notice was issued to the appellant. Its reply was considered alongwith the oral statement before the Committee. The Committee found that two violations were

committed by the appellant, while it was absolved from the third of the charge.

3. So far as the charge of collection of margin for trading under the margin trading facility is concerned, 14 sample instances were considered for considering the securities other than group one activity. Additionally 10 sample instances wherein securities other than group one were considered for trading under the margin trading facility. The appellant pointed out before the Committee that some securities pertaining to a client were forming part of group one securities at the time of trade. With respect to the remaining securities the noticee submitted that these securities comprised of bond and debentures which were accepted as collateral for margin trading facility as per the internal risk policy having credit rating of AA, AAA and AAA/stable.

4. The Committee of the respondent found that while the part of the securities were in fact group one

security at the time of accepting them, another group of 10 securities in the nature of bonds and debentures as detailed supra cannot be accepted as they do not fall under the group one securities as defined by Securities and Exchange Board of India (hereinafter referred to as 'SEBI') vide its circular no.SEBI/HO/MRD/DP/CIR/P/2016/ 135 dated 16th December, 2016, SEBI circular no. CIR/MRD/DP/54/2017 dated 13th June, 2017 and circular no.NSE/COMP/35125 dated 15th June, 2012. In the circumstances penalty of Rs.5 lakhs on this count was imposed.

5. Another violation with which the appellant was charged was non adherence to leverage and exposure limit while granting the margin trading facility. It was alleged that the appellant had granted an excess exposure on aggregate basis at member level to the tune of Rs.1,75,09,72,380. This exposure was calculated as the Committee of the respondent excluded the funds borrowed by the

appellant from the sources which were not approved by SEBI vide its circular no. CIR/MRD/DP/54/2017 dated 13th June, 2017 and circular no.CIR/MRD/DP/ 86/2017 1st August, 2017 (hereinafter called as the circular dated 13th June, 2017 and circular dated 1st August, 2017).

The appellant's explanation was that while the circular dated 1st August, 2017 permits the broker to avail borrowing of fund for the above purposes from the promoter it had availed loan from its group entity namely Edelweiss Rural and Corporate Services Ltd. (hereinafter referred to as 'ERCSL'). Said ERCSL as well as the appellant are subsidiaries of Edelweiss Financial Services Ltd. The appellant has therefore contended that if the SEBI circular dated 1st August, 2017 is read as permitting loan from the promoter group also, there would not be any violation. The respondent's Committee however observed that the said circular permits borrowing from the promoter and the

definition of the promoter as found in section 269 of the Companies Act does not include group entity. The submissions of the appellant therefore was not accepted and, therefore, a penalty of Rs.1,75,10,000 was imposed on this count. Hence the present appeal.

6. Heard Mr. Somasekhar Sundaresan, Advocate assisted by Mr. Sameer Pandit, Ms. Krina Gandhi, Advocates and Ms. Kamala Kantharaj, Authorised Representative for the appellant and Mr. Venkatesh Dhond, Senior Advocate assisted by Mr. S. Vivek, Mr. Aditya Sikka, Ms. Drishti Das, Mr. Siddhant Sattur, Advocates for the Respondent.

7. The main thrust of the argument of Mr. Somasekhar Sundaresan was against the imposition of penalty of Rs.1,75,10,000 upon non acceptance of the submissions of the appellant that the borrowing from the group entity i.e. the promoter group should be accepted. On the other hand, learned counsel for the respondent submitted that

the very circular dated 1st August, 2017 refers to the provisions of the Companies Act which does not prescribe any definition of promoter group and the circular also permits availment of loan from promoters only.

8. SEBI's circulars dated 13th June, 2017 and 15th June, 2017 provides that a stock broker may provide margin facility by using own funds or borrowed funds from scheduled commercial banks and/or NBFC regulated by Reserve Bank of India. It specifically provides that a stock broker cannot be permitted to borrow funds from any other sources.

These restrictions were relaxed vide next of the circulars dated 1st August, 2017 and 3rd August, 2017 which modified the earlier provisions of para 14 and prescribed as under:-

> *"3. Accordingly, it is clarified that Stock brokers may borrow funds by way of issuance of CP and by way of unsecured long term loans from their promoters and directors. The borrowing by way of issuance of CPs shall be subject to compliance with appropriate RBI Guidelines. The borrowing by way of unsecured long terms loans from the*

promoters and directors shall be subject to the appropriate provisions of Companies Act.
4. A stock broker shall not be permitted to borrow funds from any other source, except the sources as sated at para 3 above."

9. Thus, vide this next of the two circulars borrowing of funds (i) by issuance of CP subject to the compliance with appropriate RBI guidelines (ii) by way of unsecured loan from promoter and directors was permitted.

10. Mr. Somasekhar submitted that no specific definition of the term "promoter" is prescribed in these two circulars. The term therefore will have to be contextually and purposefully interpreted to include even the members of the promoter group. Even if the definition provided in the Companies Act, 2013 of the promoter is considered, it should be kept in mind that the defining section starts with the caveat that the definition should be read unless the context requires otherwise. He submitted that the context provided by these two circulars is one of widening and liberalizing the sources of borrowing

for the purposes of margin trading. These facts are required to be taken into consideration. The appellant as well as the ERCSL are the subsidiaries of Edelweiss Financial Services Ltd. The respondent's Committee also noted in the impugned order that ERCSL as well as the appellant are 100% subsidiary of EFSL. Had the appellant borrowed the funds from EFSL, the respondent's Committee could not have any grievance. On the other hand as the appellant has borrowed the funds from ERCSL which is also 100% subsidiary of EFSL, the purport of the circular is not taken into consideration by the Committee. To apply a simile a son obtaining a loan from his father is permitted, but obtaining a loan from the pocket of the brother who is fully funded by the father has caused the respondent Committee to penalize the appellant to the tune of Rs.1,75,10,000. In the circumstances, he submitted that the term promoter as used in the circular will have to be read in it's context. In fact SEBI which

had issued the above circulars had in various regulations like Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 (for short 'ICDR, 2018'), Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("LODR 2015' for short), Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ('Takeover Regulation' for short), Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015 had covered the promoter group along with the promoter while making the provisions of charging sections etc.

11. In order to buttress this submissions Mr. Somasekhar relied on the ratio of following four authorities from the Supreme Court and also of the order of a Whole Time Member of SEBI in the matter of Xchanging Solutions India Ltd vide order

dated 28th January, 2020. The authorities relied on are as under.

(a) *The Vanguard Fire and General Insurance Co. Ltd. vs. Fraser and Ross and Another. [AIR 1960 SC 971]*.

(b) *K.P. Varghese vs. The Income Tax Officer, Ernakulam and Anr. [(1981) SCC (4) 173]*.

(c) *Smt. Pushpa Devi & Ors vs. Milkhi Ram [(1990) 2 SCC 134]*.

(d) *K. V. Muthu vs Angamuthu Ammal [(1997) 2 SCC 53]*.

12. On the other hand Mr. Mr. Venkatesh Dhond, learned senior counsel for the respondent submitted that the circular itself prescribes that borrowing of funds from promoter is permitted. The circular further also referred to the provisions of the Companies Act. The circular would show that while earlier the borrowing of fund was limited only from the source of scheduled bank and NBFC, further permission was granted to avail loan from promoter and by way of corporate borrowing under certain specified conditions. He further submitted that the definition of promoter and promoter group

found in some of the Regulations of SEBI has no role to play in the present scenario. The purpose of defining promoter and promoter group in those Regulations is to regulate various entities, as regards the issue of capital, disclosures, takeover, prevention of insider trading etc. It was therefore submitted that the appeal be dismissed.

13. In the case of the Vanguard Fire and General Insurance Co. Ltd. cited supra the question related to the interpretation of section 33 of the Insurance Act, which provides for inspection of the affairs of an insurer by an authority. The term ‘insurer’ was defined as an entity carrying on the business of insurance. The authorities under section 33 of the Insurance Act decided to carry inspection of the appellant’s affairs who had already closed its business. The appellant ther in therefore argued that since it did not remain insurer as per the definition of the Insurance Act, no inspection can be carried. The inspection was contempleted regarding the past

business of the appellant. In this context the apex court observed that the court is required not only to look at the word but also to look at the context, the collocation and the object of such words relating to such matters and interpret the meaning. Taking into consideration the context the apex court found that the literal meaning of the term of the definition 'insurer' found in the insurance Act will have to be expanded to mean that it would include the entity who was insurer in the past.

In the case of K.P. Varghese the issue was regarding assessment of the tax on transfer of a property by assesse for the purpose of capital gains. Section 52 (2) of the Income Tax Act 1961 provided that if in the opinion of the Income Tax Officer, fair market value of a transferred property as on the date of transfer exceeds the full value of the consideration declared by the assessee above 15 percent, then the fair market value would be considered for assessment. Considering the fact that the actual

transfer may take effect after several years of the agreement, marginal notes appended to the Section and a contemporaneous circular, again a purposive interpretation was invoked by the Supreme Court. It was held that the provisions of the Section would be applicable only if the assessee makes an understatement regarding the value of the property.

14. In the case of Pushpa Devi cited supra possession of a shop premises was sought by the landlord on the ground of non-deposit of the arrears of rent by the tenant in the Court.. In that case a common counsel for the tenant as well as the alleged sub-tenant had deposited the rent in the court. It was therefore argued by the landlord that since the rent was not deposited by the tenant exclusively, there was a default and hence eviction on this ground was sought. The alleged sub-tenant had claimed that in fact he was the co-tenant being a partner in the partnership firm. In this context again

the purposive interpretation of the term tenant was made by the Supreme Court.

In the case of K. V. Muthu cited supra successor of the landlord – the widow- sought possession of the tenanted premises for bona fide occupation of the same by a foster son. The term family was defined in the Tamil Nadu Buldings (Lease and Rent Control) Act, 1960 as a nuclear family which did not include a foster son for whom the bonafide occupation was sought. The documents on record showed that landlord's brother's son was reared by the deceased original landlord and even the property was bequeathed to him. In those circumstances the Supreme Court was required to interpret the word family as defined in the said Act. The Supreme Court made a purposive interpretation of the term family and declared that a foster son would also include in the same.

In the case of Xchanging Solutions Ltd. the learned Whole Time Member of SEBI relied on the ratio of

Pushpa Devi cited supra to interpret the term frequently traded shares.

15. In our view the first principle of the interpretation to be applied is that there shall be no interpretation of statute. It means that a literal interpretation of statute is required to be made unless the context requires otherwise or unless it is contrary to the intent of the legislation upon consideration of the whole scheme of the relevant legislation.

16. In the present case the earlier circulars of the SEBI strictly permitted availing loan from the scheduled commercial bank and/or NBFC only. This provision was liberalized by the next of the circular which provided for borrowing by way of unsecured long term loan from promoter and by way of issuance of Commercial Paper (CP).

The appellant had secured loan not from the promoter but from the group entity

17. Grafting of the definitions of other SEBI regulations in the circulars cannot be made by making any interpration in the above circumstances. The object and purpose of those Regulation is to regulate/cover various entities including promoter and promoter group.

Regulation 2(1)(oo) of ICDR Regulations, 2018, which is adopted in other above referred Regulations defines promoter as under.

> ***"2. Definitions***
>
> *(1) In these regulations, unless the context otherwise requires:*
>
> *(oo) "promoter" shall include a person:*
>
> *i) who has been named as such in a draft offer document or offer document or is identified by the issuer in the annual return referred to in section 92 of the Companies Act, 2013; or*
>
> *ii) who has control over the affairs of the issuer, directly or indirectly whether as a shareholder, director or otherwise; or*
>
> *iii) in accordance with whose advice, directions or instructions the board of directors of the issuer is accustomed to act:*
>
> *Provided that nothing in sub-clause (iii) shall apply to a person who is acting merely in a professional capacity;*

Provided further that a financial institution, scheduled commercial bank, foreign portfolio investor other than Category III foreign portfolio investor, mutual fund, venture capital fund, alternative investment fund, foreign venture capital investor, insurance company registered with the Insurance Regulatory and Development Authority of India or any other category as specified by the Board from time to time, shall not be deemed to be a promoter merely by virtue of the fact that twenty per cent or more of the equity share capital of the issuer is held by such person unless such person satisfy other requirements prescribed under these regulations;

18. Regulation 2(1)(pp) defines promoter group as under:

"(pp) "promoter group" includes:

i) the promoter;

ii) an immediate relative of the promoter (i.e. any spouse of that person, or any parent, brother, sister or child of the person or of the spouse); and

iii) in case promoter is a body corporate:

a) a subsidiary or holding company of such body corporate;

b) any body corporate in which the promoter holds twenty per cent. or more of the equity share capital; and/or any body corporate which holds twenty per cent. or more of the equity share capital of the promoter;

c) any body corporate in which a group of individuals or companies or combinations thereof acting in concert, which hold twenty

per cent. or more of the equity share capital in that body corporate and such group of individuals or companies or combinations thereof also holds twenty per cent or more of the equity share capital of the issuer and are also acting in concert; and

iv) in case the promoter is an individual:

a) any body corporate in which twenty per cent. or more of the equity share capital is held by the promoter or an immediate relative of the promoter or a firm or Hindu Undivided Family in which the promoter or any one or more of their relative is a member;

b) any body corporate in which a body corporate as provided in (A) above holds twenty per cent. or more, of the equity share capital; and

c) any Hindu Undivided Family or firm in which the aggregate share of the promoter and their relatives is equal to or more than twenty per cent. of the total capital;

v) all persons whose shareholding is aggregated under the heading "shareholding of the promoter group":

Provided that a financial institution, scheduled bank, foreign portfolio investor other than Category III foreign portfolio investor, mutual fund, venture capital fund, alternative investment fund, foreign venture capital investor, insurance company registered with the Insurance Regulatory and Development Authority of India or any other category as specified by the Board from time to time, shall not be deemed to be promoter group merely by virtue of the fact that twenty per cent or more of the equity share

capital of the promoter is held by such person or entity:

Provided further that such financial institution, scheduled bank, foreign portfolio investor other than Category III foreign portfolio investor, mutual fund, venture capital fund, alternative investment fund and foreign venture capital investor insurance company registered with the Insurance Regulatory and Development Authority of India or any other category as specified by the Board from time to time shall be treated as promoter group for the subsidiaries or companies promoted by them or for the mutual fund sponsored by them;"

19. The reading of the above definitions would show that the promoter group includes the promoter and other entities as enumerated therein. While the promoter group is a genus, promoter is one of the specie. The appellant wants that the entire genus of the promoter group should be grafted in the circular dated 1st August, 2017.

At the time of obtaining loan from the group entity the appellant was very well aware that the circular does not permit the same. The circular had only opened a chink for borrowing from the promoter or by way of CP only in certain circumstances. The context therefore does not require widening any

scope of the term ‘promoter’ employed in the said circular. The finding of the Committee on this count therefore requires no interference.

However, as regards quantum of the penalty on this count, in our view in the facts and circumstances that when borrowing of money in the nature of CP is permitted, vide the circular dated 1st August, 2017, the appellant has merely availed loan from one of its group entity who was 100% subsidiary of the promoters of the appellant. Therefore according to us though there is a violation on the part of the appellant, the penalty of Rs.1,75,10,000 on this count at the rate of 1% of the exact amount involved is excessive. Considering all the above facts, in our view a penalty of Rs.25 (Twenty Five) lakhs on this count would meet the ends of the justice. Hence the following order.

20. The appeal is partly allowed without any order as to costs. The appeal to the extent of levying penalty of Rs.5 lakhs for considering the collection of

margin for trading under the margin trading facility by way of securities other than group one is hereby confirmed. However, the penalty of Rs.1,75,10,000 for non-adherence to the leverage and exposure limit is hereby set aside. Instead it is hereby directed that the penalty of Rs.25 lakh also shall be paid by the appellant on this count.

21. The present matter was heard through video conference due to Covid-19 pandemic. At this stage it is not possible to sign a copy of this order nor a certified copy of this order could be issued by the registry. In these circumstances, this order will be digitally signed by the Private Secretary on behalf of the bench and all concerned parties are directed to act on the digitally signed copy of this order. Parties will act on production of a digitally signed copy sent by fax and/or email.

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Date: 2021.01.07 15:43:21 +05'30'

Justice TarunAgarwala
Presiding Officer

Dr. C.K.G. Nair
Member

Justice M.T. Joshi
Judicial Member

7.1.2021
RHN