NWML/SEC/2024/47

December 16, 2023

The Manager,
Listing Department,
BSE Limited,
Phiroze Jeejeebhoy Tower,
Dalal Street,
Mumbai 400 001.
BSE Scrip Code: 543988

The Manager,
Listing Department,
National Stock Exchange of India Ltd.,
Exchange Plaza, 5 Floor, Plot C/1, G Block, Bandra - Kurla Complex, Bandra (E),
Mumbai 400 051.
NSE Symbol: NUVAMA

Subject: - Disclosure under Regulation 30 of Securities Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("Listing Regulations")

Dear Sir(s) / Madam(s),

In accordance with the provisions of Regulation 30 of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, we would like to inform you that the Securities Appellate Tribunal vide order dated December 15, 2023, dismissed the appeal filed by Nuvama Clearing Services Limited, formerly known as Edelweiss Custodial Services Ltd. ("Nuvama Clearing"), a wholly owned subsidiary of the Company, against the order passed by Member and Core Settlement Guarantee Fund Committee of NSE Clearing Ltd. The order was received by Nuvama Clearing on December 15, 2023 and is enclosed herewith.

Nuvama Clearing is evaluating all legal options in the matter, including but not limited to filing an appeal with the Supreme Court of India. Nuvama Clearing has already earmarked with NSE Clearing Ltd. a sum of Rs. 236 crores in this regard and believes this will have no material impact on the Company.

Kindly take the same on record.

Thanking you,
Yours faithfully,

For Nuvama Wealth Management Limited
(formerly known as Edelweiss Securities Limited)

Sneha Amit Patwardhan
Digitally signed by Sneha Amit Patwardhan
Date: 2023.12.16 14:53:24 +05'30'

Sneha Patwardhan
Company Secretary and Compliance Officer

Encl.: as above

BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Date of Hearing : 10.02.2023
Date of Decision : 15.12.2023

Misc. Application No. 422 of 2020
And
Misc. Application No. 512 of 2020
(Stay Application)
And
Misc. Application No. 585 of 2020
And
Misc. Application No. 736 of 2021
And
Misc. Application No. 1192 of 2021
And
Misc. Application No. 1353 of 2021
And
Misc. Application No. 1354 of 2021
And
Misc. Application No. 134 of 2022
And
Misc. Application No. 213 of 2022
And
Misc. Application No. 221 of 2022
And
Appeal No. 441 of 2020

Edelweiss Custodial Services Ltd.
Edelweiss House,
Off. C.S.T Road, Kalina,
Mumbai - 400 098. ….. Appellant

Versus

1. NSE Clearing Ltd.

Exchange Plaza, Block G, C 1,
Bandra Kurla Complex, Bandra (East),
Mumbai - 400 051.

2. VRise Securities Pvt. Ltd.
Office No. 3, 1st Floor, Plot No. 57/58,
S M Jivaji Dadabhai Bldg.,
Nagdevi Street, Mandvi,
Mumbai – 400 003.

3. National Stock Exchange of India Ltd.
Exchange Plaza, Block G, C 1,
Bandra Kurla Complex, Bandra (East),
Mumbai - 400 051. … Respondents

Mr. Janak Dwarkadas, Senior Advocate and Mr. Gaurav Joshi, Senior Advocate with Mr. Sameer Pandit, Ms. Krina Gandhi, Mr. Anmol Menon, Advocates i/b. Wadia Ghandy & Co. for the Appellant.

Mr. Pesi Modi, Senior Advocate with Mr. Neville Lashkari, Mr. Yogesh Chande, Ms. Shweta Ojha, Ms. Preeti Kapany, Advocates i/b Shardul Amarchand Mangaldas and Co. for the Respondent Nos. 1 (NSE Clearing).

Mr. Venkatesh Dhond, Senior Advocate with Mr. Viraj Maniar, Ms. Sneha Patil, Mr. Saurabh Kshirsagar, Advocates i/b Maniar Srivastava Associates for the Respondent Nos. 2 (V Rise Securities) .

Mr. Venkatesh Dhond, Senior Advocate with Mr. Viraj Maniar, Ms. Sneha Patil, Mr. Saurabh Kshirsagar, Advocates i/b Maniar Srivastava Associates for the Respondent Nos. 3 (NSEIL) .

Ms. Mitravinda Chunduru, Advocate with Mr. Ravichandra Hegde, Ms. Svadha Shankar, Advocates i/b Parinam Law Associates in Misc. Application No. 512 of 2020.

Mr. Zain J. Shroff, Advocate i/b M/s Y & A Legal for the Intervener (Intervention Application No. 585 of 2020).

Mr. Kunal Katariya, Advocate with Ms. Ashmita Goradia, Ms. Shraddha Jadhav, Advocates i/b Aagam Doshi & Co. in Misc. Application No. 1353 of 2021 and Misc. Application No. 1354 of 2021.

Mr. Kamal R. Bulchandani (in person) i/b. Kamal & Co. for the Interveners in Misc. Application Nos. 134, 213, 221 of 2022.

With
Misc. Application No. 1346 of 2021
(Harsh Rohitbhai Patel)
And
Misc. Application No. 482 of 2020
(Rajiv Agarwal)
And
Misc. Application No. 99 of 2020
(Ashish Shah)
And
Appeal No. 80 of 2020

Edelweiss Custodial Services Ltd.
Edelweiss House,
Off. C.S.T Road, Kalina,
Mumbai - 400 098. ….. Appellant

Versus

1. NSE Clearing Ltd.
   Exchange Plaza, Block G, C 1,
   Bandra Kurla Complex, Bandra (East),
   Mumbai - 400 051.

2. VRise Securities Pvt. Ltd.
   Office No. 3, 1st Floor, Plot No. 57/58,
   S M Jivaji Dadabhai Bldg.,
   Nagdevi Street, Mandvi,
   Mumbai – 400 003.

3. National Stock Exchange of India Ltd.
   Exchange Plaza, Block G, C 1,
   Bandra Kurla Complex, Bandra (East),
   Mumbai - 400 051. …… Respondents

Mr. Gaurav Joshi, Senior Advocate with Mr. Sameer Pandit, Ms. Krina Gandhi, Mr. Anmol Menon, Advocates i/b Wadia Ghandy & Co. for the Appellant.

Mr. Pesi Modi, Senior Advocate with Mr. Nihar Mody, Mr. Yogesh Chande, Ms. Shweta Ojha, Ms. Preeti Kapany, Advocates i/b Shardul Amarchand Mangaldas and Co. for the Respondent Nos. 1 (NSE Clearing).

Mr. Viraj Maniar, Advocate with Ms. Sneha Patil, Mr. Saurabh Kshirsagar, Advocates i/b Maniar Srivastava Associates for the Respondent Nos. 2 (V Rise Securities) .

Mr. Viraj Maniar, Advocate with Ms. Sneha Patil, Mr. Saurabh Kshirsagar, Advocates i/b Maniar Srivastava Associates for the Respondent Nos. 3 (NSEIL) .

Mr. Paras Parekh, Advocate with Mr. Samyak Pati, Advocate i/b Parinam Law Associates for the Intervenor in the Misc. Application No. 99 of 2020 in Appeal No. 80 of 2020.

Mr. Kumaresh B. Purohit, Advocate with Mr. Prithvish B. Purohit, Advocate i/b. by Purohit & Purohit for the Intervenor in the Misc. Application No. 482 of 2020 in Appeal No. 80 of 2020.

Mr. Robin Shah, Advocate with Mr. Rushin Kapadia, Advocate i/b Bodhi Legal for the Intervener (MA No. 1346 of 2021).

With
Appeal No. 370 of 2021

Yes Bank Ltd.
YES Bank Tower,
15th Floor, IFC 2,
Elphinstone Road (W)
Mumbai - 400 013. …Appellant

Versus

1. NSE Clearing Ltd.
   Exchange Plaza, Block G, C 1,
   Bandra Kurla Complex, Bandra (East),
   Mumbai - 400 051.

2. National Stock Exchange of India Ltd.
   Exchange Plaza, Block G, C 1,
   Bandra Kurla Complex, Bandra (East),
   Mumbai - 400 051. …Respondents

Mr. Mustafa Doctor, Senior Advocate with Ms. Vidhi Jhawar, Mr. Pulkit Sukhramani, Mr. Deepank Anand, Advocates i/b J. Sagar Associates for the Appellant.

Mr. Pesi Modi, Senior Advocate with Mr. Neville Lashkari, Mr. Sachin Chandarana, Mr. Akshay Dhayalkar, Advocates i/b MKA & Co. for Respondent Nos. 1. (NSE Clearing Ltd.).

Mr. Rashid Boatwalla, Advocate and Mr. Juan D'Souza, Advocate i/b MKA & Co. for Respondent Nos. 2 (NSEIL).

With
Misc. Application No. 1407 of 2021
And
Appeal No. 757 of 2021

SMC Global Securities Ltd.
11/6B, Shanti Chamber,
Pusa Road, New Delhi – 110005. ….. Appellant

Versus

1. NSE Clearing Ltd.
   Exchange Plaza, Block G, C 1,
   Bandra Kurla Complex, Bandra (East),
   Mumbai - 400 051.

2. National Stock Exchange of India Ltd.
   Exchange Plaza, Block G, C 1,
   Bandra Kurla Complex, Bandra (East),
   Mumbai - 400 051.

3. Yuvraj Securities
   Prop. Mr. Vijay Kumar Goel
   9, Weston Street,
   Siddha Weston,

2nd Floor, Room No. 207 – 208,
Kolkata – 700012. … Respondents

Mr. Prakash Shah, Advocate with Mr. Kushal Shah, CA i/b Prakash Shah & Associates for the Appellant.

Mr. Pesi Modi, Senior Advocate with Mr. Neville Lashkari, Mr. Sachin Chandarana, Mr. Akshay Dhayalkar, Advocates i/ MKA & Co. for the Respondent Nos. 1. (NSE Clearing Ltd.)

Mr. Rashid Boatwalla, Advocate with Mr. Juan D'Souza, Advocate i/b Manilal Kher Ambalal & Co. for the Respondent Nos. 2. (NSEIL)

None for the Respondent Nos. 3. (Yuvraj Securities)

CORAM : Justice Tarun Agarwala, Presiding Officer
Ms. Meera Swarup, Technical Member

Per : Justice Tarun Agarwala, Presiding Officer

1. Four appeals have been filed against different orders passed by the Member and Core Settlement Guarantee Fund Committee (hereinafter referred to as 'Committee') of NSE Clearing Ltd. (hereinafter referred to as 'NCL') directing the appellants to reinstate the securities which were disposed of in contravention of the Securities and Exchange Board of India (hereinafter referred to as 'SEBI') circular and NCL Regulations within a period of 15 days

failing which an amount equivalent to the value of securities as on the 16th day of the closing price on National Stock Exchange of India Ltd. (hereinafter referred to as 'NSE') mark-up value of 5% shall be blocked from the available collateral of the appellant with NCL.

2. The issue is common in all the appeals and, therefore, these four appeals are being taken up together. For facility, the facts stated in Appeal No. 441 of 2020 shall be taken into consideration.

3. Edelweiss Custodial Services Ltd. now known as Nuvama Clearing Services Ltd. (hereinafter referred to as 'Edelweiss') is a member of NCL and is registered as a Professional Clearing Member (hereinafter referred to as 'PCM') since 2018. Edelweiss as a PCM provides clearing and settlement services to brokers / trading members. The appellant Edelweiss is not a member of the stock exchange i.e. NSE nor carries out any trading activities on the exchange either for itself or on behalf of any client.

4. Anugrah Stock & Broking Ltd. (hereinafter referred to as 'Anugrah') was a broker and trading member of various stock exchanges including NSE. Anugrah executed trades on the stock exchanges for its client's across various segments. Anugrah, in turn, was the client of the appellant Edelweiss who provided clearing

services to Anugrah only for the trades executed on the Future & Options (hereinafter referred to a 'F&O') segment of the NSE in accordance with the bye-laws of NCL. The appellant Edelweiss collected collaterals from Anugrah towards Anugrah's margin requirement for settlement of trades on an aggregate basis. These collaterals were transferred directly by Anugrah to the appellant Edelweiss. Most of the collaterals were in the form of shares.

5. Between January 15, 2020 and June 2, 2020, Anugrah failed to pay its dues to the appellant Edelweiss on multiple occasions. To recover these dues, the appellant Edelweiss sold the collaterals furnished by Anugrah to the tune of Rs. 460.32 crore and applied the proceeds to meet Anugrah's clearing obligation towards NCL. All such proceeds were duly shown as credit entries in Anugrah's ledger account with the appellant Edelweiss. The collaterals sold were utilized by Edelweiss for the purpose of meeting the closing obligation of Anugrah. On April 2, 2020, Edelweiss received an email from NSE advising the appellant Edelweiss to perform adequate due diligence while handling clients' assets and ensure that client's securities were utilized only for meeting the respective clients' obligations. On July 13, 2020, Anugrah terminated its relationship with the appellant Edelweiss and shifted to another

clearing member. On August 3, 2020, NSE passed an order disabling Anugrah's terminals. On September 19, 2020, NCL issued a show cause notice to the appellant Edelweiss alleging that it had failed to carry out due diligence and to ascertain whether there were any debit balances for the said clients before liquidation of the securities. The show cause notice called upon the appellant Edelweiss to show cause as to why appropriate disciplinary proceedings in terms of Rule 1 and Rule 2 of the Chapter V of Rules of NCL (F&O) should not be taken for the non-compliances mentioned in the show cause notice.

6. The appellant Edelweiss denied the allegations and contended that they had committed no wrong. The Committee after considering the submissions, passed the impugned order dated October 20, 2020 holding that the appellant Edelweiss had failed to perform adequate due diligence while handling client securities and failed to ensure that the clients' securities were only utilized for meeting the clients' obligations and, therefore, the appellant Edelweiss was in contravention of Clause 1 and Clause 2 read with Clause 3(1)(b) and 3(1)(c) of Chapter V of NCL Rules. The Committee by the impugned order directed the appellant Edelweiss to reinstate the securities by procuring the same from the market. After the passing of the impugned order, NSE sent two e-mails on October 30, 2020

and November 13, 2020 providing a list of securities to be reinstated by the appellant Edelweiss.

7. Appeal No. 80 of 2020 has been filed by Edelweiss Custodial Services Ltd. challenging the order dated February 13, 2020. The facts in Appeal No. 80 of 2020 are more or less similar except that the trading member / client of the appellant Edelweiss was VRise Securities Pvt. Ltd. (hereinafter referred to as 'VRise') who defaulted and accordingly, the appellant Edelweiss sold off the securities of the client of VRise for Rs. 22 crore to recover the outstanding dues of VRise proprietary trading. By the impugned order, the Committee directed the appellant Edelweiss to reinstate / buy and return the shares of the client whose shares were wrongly sold off.

8. Appeal No. 757 of 2021 SMC Global Securities Ltd. (hereinafter referred to as 'SMC Global') is a Clearing Member (hereinafter referred to as 'CM') duly registered with NCL. The concerned trading member whose trades were cleared by the SMC Global is Yuvraj Securities (hereinafter referred to as 'Yuvraj'). The Committee by the impugned order found that the appellant SMC Global had wrongly sold off the securities of Rs. 75.74 lakh of the client of the trading member for the dues of the trading member

despite being aware that the same were client's securities. The Committee accordingly by an impugned order dated December 7, 2021 directed the appellant SMC Global to reinstate / buy and return the shares.

9. In Appeal No. 370 of 2021, Yes Bank Ltd. (hereinafter referred to as 'Yes bank') is a Clearing Member registered with NCL and the trading member whose trades were cleared by the appellant Yes Bank was Action Financial Services ((India) Ltd. (hereinafter referred to as 'Action Financial'). The appellant Yes Bank wrongly sold off the securities of the client of the Action Financial worth of Rs. 1.95 crore to clear the outstanding dues of the proprietary trades of Action Financial in spite of knowing that the securities were of the clients of Action Financial. By the impugned order dated May 3, 2021, the Committee directed the appellant Yes Bank to reinstate / buy and return these shares of clients who had no outstanding liability and whose shares were wrongly sold off by the appellant Yes Bank.

10. The appellants denied the charges and contended that they had not misutilised the client securities. The appellants contended that they are Professional Clearing Member / Clearing Member and

have no role to play in the execution of trades by a trading member on its own behalf or on behalf of the trading members' clients and that the appellants only clears and settles trades executed by the constituents, namely, the trading member. It was contended that the appellants do not have any relationship or dealings of whatsoever kind with the end clients of the trading members. It was urged that the word "constituent" which is referred to in the bye-laws of NCL can only mean that a trading member with whom the appellants have an agreement and it cannot mean to include the end clients of the trading member. It was also urged that once shares were transferred by the clients of the trading member to the trading member and the trading member transferred the same to the appellants, the clients of the trading member ceased to have any legal or beneficial ownership on all those particular shares. It was contended that the appellant liquidated the collaterals placed by the trading member and it was done so as to recover the debit balance of the trading member. Since the appellants had used the trading members collaterals only to meet the trading members obligation, the appellants were fully compliant with the obligations relating to handling of collateral under the rules, bye-laws and regulations of NCL. It was urged that the circulars relied upon in the show cause notice only applies to a trading

member and is not applicable to the appellants who are PCM / CM. It was further contended that the clearing member - trading member agreement entered by the appellants with the trading member did not require the appellants to monitor margin or liquidate collaterals based on obligations of the trading members client.

11. The Committee after considering the matter found that the appellants had entered into an agreement with the trading member which was known as clearing member - trading member agreement. The appellants had also obtained an undertaking from the trading member with respect to the securities submitted to the appellants as collateral. The undertaking by the trading member clearly indicated that the securities / funds of the client were being placed before the appellants as collateral as per the provision of SEBI circular dated September 26, 2016. The trading member further gave an undertaking that the securities / funds of their client which are placed as collateral with the appellants would only be utilized for the respective client position and not for other client or for own purpose.

12. The Committee further found that the appellants had also uploaded to NCL on a weekly basis, the client-wise and ISIN wise details of the non-cash securities collateral placed by the trading

member. The Committee, therefore, concluded that the appellants were fully aware that the securities that were disposed of were of the client securities as this information was contained in the upload made by the appellants to NCL and, therefore, it was not open to the appellants to contend that they were not aware that the said securities were in fact belonged to the clients of the trading member. The Committee also found that in view of the undertaking given by the trading member, it was clear that the appellants knew that the securities belonged to the clients of the trading member and in spite of knowing that the securities of a client could only be utilized towards the respective client position still sold the client securities to meet the obligation of the trading member proprietary trades. The Committee found that the appellants had violated the SEBI circular dated April 17, 2008, NSE circular dated April 21, 2008 and SEBI circular dated June 20, 2019 as well as Regulation 10.2.4 of the NCL F&O Segment Regulations and, further, found the appellants not adhering to NCL and NSE directives and, consequently, violating Clause 1 and Clause 2 read with Clause 3(1)(b) and 3(1)(c) of Chapter V of NCL Rules.

13. We have heard Mr. Janak Dwarkadas, the learned senior counsel and Mr. Gaurav Joshi, the learned senior counsel with Mr.

Sameer Pandit, Ms. Krina Gandhi, Mr. Anmol Menon, the learned counsel for the appellant Edelweiss and Mr. Mustafa Doctor, the learned senior counsel with Ms. Vidhi Jhawar, Mr. Pulkit Sukhramani, Mr. Deepank Anand, the learned counsel for the appellant Yes Bank and Mr. Prakash Shah, the learned counsel with Mr. Kushal Shah, CA for the appellant SMC Global and Mr. Pesi Modi, the learned senior counsel with Mr. Nihar Mody, Mr. Neville Lashkari, Mr. Yogesh Chande, Ms. Shweta Ojha, Ms. Preeti Kapany Mr. Neville Lashkari, Mr. Sachin Chandarana, Mr. Akshay Dhayalkar, the learned counsel for the respondent NCL and Mr. Venkatesh Dhond, the learned senior counsel with Mr. Viraj Maniar, Ms. Sneha Patil, Mr. Saurabh Kshirsagar, the learned counsel for the respondent VRise and NSE and Mr. Rashid Boatwalla, the learned counsel with Mr. Juan D'Souza, the learned counsel for the respondent NSE. We have also heard the interveners.

14. The contention of the appellant Edelweiss is, that under the bye-laws of NCL a PCM is not a CM and, therefore, the circulars issued by SEBI / NSE / NCL are not applicable. It was also urged that the appellants being a PCM or a CM had no relationship with the end client of the trading member and, therefore, the securities that were provided by the trading member were his and which had been

sold by the appellants to meet its obligation and such sale of the securities was not violative of any Rules, Regulation or circular. Further, the circulars which have been relied upon in the show cause notice and in the impugned orders only applies to brokers and are not applicable to the PCM / CM. Further, there is no power under the bye-laws of NCL to issue directions for reinstatement of the securities and, therefore, the direction to restitute / reinstate the shares was wholly illegal and without jurisdiction. It was also urged that the impugned order also goes beyond the scope of the show cause notice and that the impugned order directing restitution was violative of Article 19(1)(g) and Article 300A of the Constitution of India. It was urged there was no misutilization of the securities of the end client of the trading member

15. On the other hand, the respondent contended that the impugned order does not suffer from any error of law. The ground raised in the appeal was never raised before the Committee. However, the Committee has the power under its bye-laws to direct restitution of the shares. It was contended that one of the principles in interpreting the securities laws, rules, regulations and bye-laws including the circulars is to enhance investors protection and to safeguard the securities checks against mischief of misappropriation

of the investor's securities and money and, consequently, the direction of the Committee was fit and proper in the circumstances of the case. It was contended that the Committee had the jurisdiction to pass orders and that the appellants cannot be allowed to get away from the misdeeds which they had committed.

16. Many interveners have filed applications seeking leave to intervene in these proceedings. These interveners were individual investors whose securities have been sold illegally by the appellants while meeting the obligations of the trading member. The interveners were heard who supported the impugned order and adopted the submissions of the respondent.

17. Before we proceed to decide the contentions raised by the parties, we find that certain admitted facts are as under :-

a. The appellants admittedly have liquidated clients' securities of the trading member worth Rs. 462.32 crore in the case of Anugrah, Rs. 22 crore in the case of VRise, Rs. 75.74 lakh in the case of Yuvraj Securities and Rs. 1.95 crore in the case of Action Financial.

b. The appellants liquidated the securities of the clients of the trading members for recovery of the dues of the trading member because of its increasing debit balance.

c. It is not disputed by the appellants that as per the details uploaded by the appellants itself to NCL, the securities sold by the appellant belonged to the clients of the trading members.

d. The appellant has not verified before selling the securities as to whether such securities belonged to the defaulting clients or not.

e. The sale of securities by the appellant without verifying as to whether the securities belonged to the defaulting clients or not has resulted in the sale of clients securities for meeting the obligation of other clients.

f. The trading member had given an undertaking to the appellants that the securities placed by him towards collaterals were the securities of the client and that the securities would only be utilized towards the respective

clients position and not for other clients or for own purpose. Therefore, the appellants were aware that the securities furnished by the trading member included the securities of the clients of the trading member.

18. In the light of the aforesaid, the contention of the appellant Edelweiss that a PCM is not a CM and, therefore, the bye-laws and the circulars mentioned in the impugned order applies only to the CM and not to PCM is untenable and cannot be accepted.

19. In this regard, the NCLs F&O Regulations stipulate as under :-

> *"**2.2 F&O Clearing Members***
>
> *"F&O Clearing Member" means a member of the Clearing Corporation and includes all categories of clearing members as may be admitted as such by the Clearing Corporation to the F&O Segment.*
>
> ***2.3 Categories of F&O Clearing Members***
>
> *"The following categories of F&O Clearing Members are specified as under :*

Self-Clearing Member

Self-Clearing Member means a member of a Specified Exchange who is admitted by the relevant authority on the Clearing Corporation as a F&O Clearing Member who may clear and settle deals executed on its own account or on account of its clients.

Clearing Member

Clearing Member means a member of a Specified Exchange who is admitted by the relevant authority on the Clearing Corporation as a F&O Clearing Member who may clear and settle the following deals:

(a) Deals executed on its own account or on account of its clients.

(b) Deals executed by other members of a Specified Exchange on their own account or on account of their clients.

Professional Clearing Member

Professional Clearing Member means a Clearing Member who is admitted by the relevant authority and who may clear and settle deals executed by its constituents. ……"

It is, therefore, clear that a PCM is nothing but a category of a CM.

20. Similarly, NCL F&O Byelaws – Chapter 1 Bye Law 6 –, *interalia,* defines a Clearing Member / CM as :-

> *"Clearing Member" means a member of the F&O segment of Clearing Corporation and includes all categories of clearing members as may be admitted as such by the Clearing Corporation, but does not denote the shareholders of the Clearing Corporation."*

21. It is also pertinent to note that at the relevant time, Securities and Exchange Board of India (Stock Brokers) Regulations, 1992 (hereinafter referred to as 'Stockbrokers Regulations') defined a CM as under :-

> *" 2(ae)*
>
> *"Clearing member" means a person having clearing and settlement rights in any recognized clearing corporation and shall include any person having clearing and settlement rights on a commodity derivatives exchange :*
>
> *Provided that such a clearing member in commodity derivatives exchange shall be required to become a member of a recognized clearing corporation from such date as may be specified by the Board."*

22. Thus, the definition itself stated that anyone having clearing and settlement rights would be a CM. In fact, it is only by a recent

amendment (w.e.f. 23.2.2022) to the Stockbrokers Regulations, that a PCM has been defined in Regulation 2(ca), but the same is only because by the Schedule to the said Regulations, a PCM is required to have a much higher networth requirement as compared to other sub-categories of CMs.

23. Shri Janak Dwarkadas, the learned senior counsel for the appellant Edelweiss Custodial Services Ltd. contended that the position of a PCM is similar to the position of Senior Counsel for whom the client is an instructing advocate and not the end client. It was, thus, suggested that the Senior Counsel is not responsible to the client. This submission, in our opinion, is patently misconceived in as much as if, in a given case, the Senior Counsel misappropriates the end client's property, he would be subjected to disciplinary proceedings before the Bar Council upon a complaint filed by the client. The Senior Counsel in such a situation cannot refuse to return the client property if so directed by the Bar Council.

24. We also find that the registration certificate granted by SEBI to Edelweiss Custodial Services Ltd. indicates that it has been registered as a CM and not as a PCM.

25. Thus, the interpretation sought by the learned senior counsel that PCM is not a CM and, therefore, the bye-laws and the circulars are not applicable to the PCM is patently erroneous and cannot be accepted.

26. The contention of the appellants that it had no contract with the end client of the trading member and that collaterals were never collected from the end clients and that it had no duty of care of the clients of the trading member and that the term 'constituents' as referred to in the circulars and bye-laws and regulations can only mean the trading member with whom the CM has an agreement is erroneous and cannot be accepted.

27. As per the SEBI circular dated September 26, 2016 all trading members had to hold client shares in a separately designated client collateral account. NSE circular dated September 27, 2019 mandated that a trading member shall maintain a collateral account for transferring both the brokers own as well as client's securities collateral to the CM. The appellants were aware that it had received the said shares from the trading members demat account which was named as "Corporate Client Collateral Account" and, therefore, the appellants knew that the collateral submitted by the trading member

contained the shares of the client which could only be used for the respective client position and could not be used for other client position or for the own position of the trading member. In addition to the aforesaid, the trading member gave an undertaking expressly stating that the securities of the clients of the trading member which are being placed as collaterals with the appellants would only be utilized towards the respective clients position and not for other clients.

28. Regulation 1.7 of the NCL F&O Segment Regulations clearly provides that as regards a CM, the terms "Clients / Constituents", include all registered constituents of trading members.

29. In view of the said circulars, rules, regulations etc., it is untenable for the appellants to contend that it had no duty of care to the clients of the trading member or that it was not aware that it was selling off the trading members clients shares.

30. In view of the aforesaid, the contention that the appellants have no concern with the client of the trading member and that they can use the clients' securities to clear the debts of the trading member is patently erroneous and cannot be accepted.

31. The contention of the appellants that the various circulars indicated in the show cause notice and considered in the impugned orders issued by SEBI, NSE or NCL only applies to the brokers and does not apply to CM and PCM cannot be accepted for the following reasons :-

i) The object, purpose and intention of the said circulars was to prevent misuse of client securities. No CM can ever contend that it is entitled to misuse clients securities and sell off the same even when there is no outstanding liability of the client. The NSE circular dated April 21, 2008 was addressed to all CM's also for compliance.

ii) It may also be noted that as per Regulation 10B and 10F of the Stockbrokers Regulations, the relevant Chapters of the said Regulations are also applicable to a CM.

iii) As per Regulation 26(xiii) of the said Stockbrokers Regulations, brokers (including a CM) can be held liable for failure to segregate the securities and / or funds of a client or for using a client's funds or securities for the purposes of any other client.

iv) Regulation 1.7 of the NCL F&O Regulations expressly states that “Clients / Constituents”, include all registered constituents of the trading members.

32. The appellants contended that at the relevant time in March 2020, there was no mechanism to monitor the clients securities and that the same was provided for by SEBI’s though subsequent circulars is incorrect and irrelevant. The NCL has applied only the law, rules, regulations and circulars as applicable at the relevant time, and the same fully justify the findings in the impugned order. The subsequent circulars only provide further improvements in the system for investor protection and to prevent misuse of clients shares by trading members and CMs, but that does not exonerate the appellants for the wilful misuse of clients shares to meet the proprietary trading dues of the trading member.

33. We also find that SEBI issued a circular dated June 28, 2019. The contention that the circular is not applicable is patently erroneous. From a perusal of the circular, we find that the subject of the circular itself states **“handling of clients securities by trading members / clearing members”.** The said circular is addressed to all trading members and CMs and stipulates that **“clients securities**

received as collateral shall be used only for meeting the respective client margin requirements". Paragraph no. 1 of the circular states as under :-

> *"1. In order to protect clients' funds and securities, the Securities Contracts (Regulation) Act, 1956 and Securities and Exchange Board of India (Stock-Brokers) Regulations, 1992 specifies that the stock brokers shall segregate securities or moneys of the client or clients and* ***shall not use the securities or moneys of a client or clients for self or for any other client****....."*

34. Therefore, the appellants contention that they sold the clients securities only for the dues of the trading member, is not relevant. The clients shares were wrongly sold off by the appellants without ensuring that it sells off the trading members clients shares only for the respective end clients obligations and, therefore, in our opinion, the clients are entitled to get back their shares as held in the impugned order.

35. Regulation 10.2.4 of the NCL Regulations states that :-

> *"No F&O Clearing Member or person associated with a F&O Clearing Member shall make improper use of constituents securities or funds."*

36. Further, Regulation 1.7 defines "client" as including all registered constituents of the trading members. Therefore, qua the appellants, the prohibition against misusing "clients" securities extends also to the clients / constituents of the trading member.

37. Thus, we find that the appellants have violated the SEBI circular of June 28, 2019 and Regulation 10.2.4 of NCL Regulations. The contention of the appellants that the Committee had no power to reinstate securities under its bye-laws and, therefore, the impugned order is without jurisdiction.

38. It was urged that the impugned order admittedly does not indicate any specific provision of NCL's rules, regulations or bye-laws that grants NCL the power to direct restitution. Instead, it claims that restitution was being directed on *"established principles of restitution in the interest of justice, equity and good conscience"* and that the same is *"implicit"* in the regulations. It was contended that restitution, is in the nature of disgorgement based on a judicial assessment of loss / unjust enrichment, and cannot be considered as a penalty. It was urged that in fact, the impugned order itself acknowledges that "restitution" does not fall within the category of a

"penalty" as it imposes a separate penalty of Rs. 1 lakh on the appellant.

39. The appellants contended that NCL traces its authority to make rules, regulations and bye-laws under the Securities Contracts (Regulation) Act, 1956 (hereinafter referred to as 'SCRA'). The bye-laws are required to be approved by SEBI and published in the Official Gazette. Rule 18 of the Securities Contract (Regulation) Rules, 1957 (hereinafter referred to as 'SCRR') read with Section 23 of the General Clauses Act, 1897 (hereinafter referred to as 'GCA') also requires that after prior publication, SEBI has to consider any objections or suggestions that may be received by such authority. It was, thus, contended that NCL has no independent power to enlarge the scope of its rules or bye-laws that are required to be framed strictly under statutory scheme prescribed under the SCRA and SCRR.

40. The appellants contended that in the present case, admittedly, both the SCN and the impugned order specifically seek to impose penal action against the appellants under Rules 1 and / or Rule 2 read with 3(1)(b) and (c) of Chapter V of Rules of NCL (F&O) segment. Chapter V is a self-contained code titled

"CHAPTER V : DISCIPLINARY PROCEEDINGS, PENALTIES, SUSPENSION AND EXPULSION". The appellants contended that a bare perusal of the Rules would make it clear that it does not contain either any specific power for restitution / disgorgement or any inherent or omnibus powers similar to what SEBI may have under Section 11B of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as 'SEBI Act'). On the contrary, under these Rules, NCL's power is restricted to the following disciplinary actions : (i) expulsion; (ii) suspension; (iii) fine / penalty with or without censure; (iv) warning; and (v) withdrawal of membership rights. These rules are not open-ended or inclusive in nature. Thus, inherent or implicit powers cannot be read into NCL's Rules / Bye-laws / Regulations.

41. It was also urged that SEBI circulars dated January 10, 2019 and July 1, 2020 which were relied by the respondent to contend that through these circulars the Committee has the power to issue direction for restitution is misplaced. It was urged that these circulars do not give any source of power to the Committee to pass orders for restitution and are irrelevant for the purpose of the case.

42. It was further urged that assuming these circulars could be treated as the source of disciplinary power, such powers can be invoked only if NCL amends its rules, regulations and bye-laws as contemplated by the circulars themselves. This is also required by the scheme of the SCRA and SCRR which prescribes the manner in which rules, regulations and bye-laws have to be framed and amended. However, NCL has not amended its rules, regulations and bye-laws to grant itself any power of restitution should such power be contemplated by the above circulars. Assuming without conceding that NCL has the power of restitution, it is submitted that restitution in law is a "gains based" remedy predicted on the theory of unjust enrichment. It can only be used to disgorge unlawful gains. The learned counsel placed reliance on a decision of the Hon'ble Supreme Court in ***Sahakari Khand Udyog Mandal Ltd. vs. Commissioner of Central Excise and Customs [(2005) 3 SCC 738]*** in which it was recognized that restitution is ordered to prevent *"retention of a benefit by a person that is unjust or inequitable."*

43. On this issue, we find that the SCRA provides the power to make bye-laws. Section 8A(4) of the SCRA states that the provisions of Section 9 shall apply to a clearing corporation, as they apply in relation to a stock exchange. Section 9(3)(b) of the SCRA,

inter-alia, provides that the bye-laws of a clearing corporation, may provide that contravention of any of the bye-laws shall render a member liable to fine, expulsion, suspension or penalty, etc.

44. The "Disciplinary Jurisdiction" of the Committee as set out in Rule 1 of Chapter V of the NCL F&O Rules, stipulates as follows :-

> *"1. DISCIPLINARY JURISDICTION*
>
> *"The relevant authority may expel or suspend and / or fine and / or penalize under censure and / or warn and / or withdraw all or any of the membership rights of a Clearing Member if he is guilty of contravention, non-compliance, disobedience, disregard or evasion of any of the Bye Laws, Rules and Regulations or of any resolutions, orders, notices, directions or decisions or rulings of the F&O segment of the Clearing Corporation or the relevant authority or of any other Committee or officer of the Clearing Corporation authorized in that behalf or of any conduct, proceeding or method of business which the relevant authority in its absolute discretion deems dishonorable, disgraceful or unbecoming a Clearing Member or inconsistent with just and equitable principles or detrimental to the interests, good name or welfare of the Clearing Corporation or prejudicial or subversive to its objects and purposes."*
>
> *2. PENALTY FOR BREACH OF RULES, BYE-LAWS AND REGULATIONS*
>
> *Every Clearing Member shall be liable to suspension, expulsion or withdrawal of all or any of his Clearing Membership rights and / or to payment of fine and / or to be censured, reprimanded or warned for contravening,*

disobeying, disregarding or wilfully evading of any of these Bye Laws, Rules and Regulations …..

"3. PENALTY FOR MISCONDUCT, UNBUSINESSLIKE CONDUCT AND UNPROFESSIONAL CONDUCT

A Clearing Member shall be liable to expulsion or suspension or withdrawal of all or any of his membership rights and / or to payment of a fine and / or penalty and / or to be censured, reprimanded or warned for any misconduct, unbusiness like conduct or unprofessional conduct as provided in the provisions in that behalf as provided herein."

45. In this regard, at the outset, we are of the opinion that one of the basic tenets of law and justice is that a party cannot be permitted to benefit from his own wrongs, and, on the other hand, an innocent party cannot be made to suffer or be deprived of his property. Further, no wrongdoer can be permitted to contend that they are entitled to take advantage of their own wrong and mis-appropriate ill-gotten gains obtained by unauthorizedly, wrongly and illegally selling shares of innocent investors / clients who had no dues or liabilities, or by selling shares in excess of their dues and liabilities.

46. Admittedly, the Committee has power to impose the penalty. The word "penalty" cannot be considered in a narrow sense and has to be taken in a broad manner. Penalty means a punishment imposed

for breaking a law, rule or contract. The word "penalty" has to be considered in a broader perspective, namely, it is not confined to imposition of a monetary compensation or fine. Other directions could be issued which would come within the ambit of 'penalty' for disobeying a rule, law or contract under the disciplinary powers as provided by the bye-laws.

47. In ***Directorate of Enforcement vs. M/s. MCTM Corporation Pvt. Ltd. & Ors. [AIR 1996 SC 1100],*** the Hon'ble Supreme Court held that the expression "penalty" is a word of wide significance. Sometimes, it means recovery of an amount as a penal measure even in civil proceedings and sometimes an exaction which is not compensatory in character is also termed as a penalty.

48. In ***State of U. P. vs. Sukhpal Singh Bal, [(2005) 7 SCC 615],*** the Hon'ble Supreme Court held :-

> *"Penalty" is a slippery word and it has to be understood in the context in which it is used in a given statute. A penalty may be the subject-matter of a breach of statutory duty or it may be the subject-matter of a complaint. In ordinary parlance, the proceedings may cover penalties for avoidance of civil liabilities which do not constitute offences against the State."*

49. In ***Pratibha Processors vs. Union of India [(1996) 11, SCC 101],*** the Hon'ble Supreme Court held :-

> *"Penalty is ordinarily levied on an assessee for some contumacious conduct or for a deliberate violation of the provisions of the particular statute."*

50. In ***Sova Ray vs. Gostha Gopal Dey [(1988) 2 SCC 134],*** the Hon'ble Supreme Court held :-

> *"The expression "penalty" is an elastic term with many different shades of meaning but it always involves an idea of punishment."*

51. In ***N. K. Jain & Ors. vs. C. K. Shah & Ors. [(1991) 2 SCC 495],*** the Hon'ble Supreme Court held :-

> *"In the common parlance the word 'penalty' is understood to mean; a legal or official punishment such as a term of imprisonment. In some contexts it is also understood to mean some other form of punishment such as fine or forfeiture for not fulfilling a contract. But in gathering the meaning of this word, the context in which this is used is significant."*

52. In Butterworths Words and Phrases, Legally Defined (3rd Edn. Page 343) the meaning of the word 'penalty' is given as that the

word 'penalty' is large enough to mean, is intended to mean, and does mean, any punishment whether by imprisonment or otherwise.

53. Blackburn, J. in ***R. vs. Smith [(1862) Le & Ca 131, 138],*** observed as under :-

> *"I consider that the word 'penalty' falls to be read in a wide popular sense, ... and I select two definitions adequately conveying that sense. The late Mr. Roberton Christie (The Encyclopedia, Vol. 11, p. 204) said : 'Penalty in the broad sense may be defined as any suffering in person or property by way of forfeiture, deprivation or disability, imposed as a punishment by law or judicial authority in respect of ... an act prohibited by statute.' The Oxford Dictionary echoes the same wide conception by referring to 'a loss, disability or disadvantage of some kind ... fixed by law for some offence'."*

54. The meaning of the word 'penalty' as given in the Collins English Dictionary, is as under :-

> *"Penalty: 1. legal or official punishment, such as a term of imprisonment. 2. some other form of punishment, such as a fine or forfeit for not fulfilling a contract. 3. loss, suffering or other unfortunate result of one's own action, error, etc. 4. Sport, games etc. a handicap awarded against a player or team for illegal play, such as a free shot at goal by the opposing team, loss of points, etc."*

55. In ***People ex rel Risso vs. Randall [58 NY 2d 265, 268 Misc. 1057],*** it was held that :-

> *"A 'penalty' may refer to both criminal and civil liability, being denied as penal retribution, punishment for crime of offence, the suffering in person, rights or property which is annexed by law or judicial decision to commission of a crime or public offence."*

56. In ***City of Fort Wayne vs. Bishop [92 NE 2d 544, 547, 228 Ind 304],*** it was observed as under :-

> *"The term 'penalty' embraces all consequences visited by law on heads of those who violate police regulations and extends to all penalties whether exigible by state in interest of community or by private persons in their own interest, even when statute is remedial as well as penal."*

57. In ***City of Cincinnati vs. Wright [67 NE 2d 358, 361, 77 Ohio App 261],*** it was noted that :-

> *"The word 'penalty' is not confined to punishment or crime; it has a broader meaning in law of contracts; it is used as contradistinguished from liquidated damages. It is also used to indicate the sum to be forfeited on breach of a bond. And in common parlance it expresses any disadvantage resulting from an act."*

58. In our view, the Committee has the power not only to suspend but can also expel or penalize a CM. In its ordinary expectation the word "penalize" will take within its fold or may embrace such directions which includes a direction for restitution of the shares. Such directions, in our opinion, is within the four corners of the disciplinary powers given to the Committee under the bye-laws. If such powers are not exercised, it will make a mockery of the entire system of protecting the interest of the investors in as much as a clearing member will knowingly sells the shares of the clients of the trading member unauthorizedly and will go scot-free. It is only to safeguard against such mis-deeds that the direction to reinstate the securities was just and proper to protect the interest of the investors whose shares have been sold unauthorizedly to settle the dues of the trading member.

59. Therefore, in our opinion, the powers of the Committee would include the power to direct that clients shares be returned to the clients, since the misuse of the clients shares is the problem created by the improper conduct which is sought to be remedied and / or reversed. It is untenable to insinuate that the Disciplinary Authority

cannot protect the investors by requiring the CM to restore / return the shares of the clients to them.

60. We are also of the opinion that if the Committee has the power to suspend trading rights, it would include the power to direct a clearing member to reverse the damage caused by unlawful sales of clients shares. In fact, the Committee has the power to suspend membership rights and, therefore, a far more stringent and onerous order could always be passed directing the membership rights to be suspended till the appellants rectifies the situation by restoring the status quo ante by returning the clients shares.

61. We also find that SEBI issued a clarificatory circular dated July 1, 2020, which is also addressed to clearing corporations, clearly stating therein that with respect to clearing members, the clearing corporations are *"…. free to initiate any other actions as may be necessary in compliance with their bye-laws / rules / regulations* ***and or to protect the interest of investors ….".*** Therefore, a duty is cast upon NCL / Committee to ensure that the investors are protected by directing the return of the shares of the respective investors as directed in the impugned order.

62. SEBI circular dated January 10, 2019, to clearing corporations, expressly states that the Committee also has powers to impose appropriate regulatory measures on CMs. Thus, a wide power has been given to the Committee to ensure proper regulation of the markets and investor protection.

63. Once it is evident that the appellants have wrongly sold off the shares of clients, it would make a mockery of disciplinary regulation and be a travesty of justice to hold that the NCL has no power to direct the appellant to reinstate and return the shares to the clients. Such a conclusion would place a premium on dishonesty and encourage brokers to misappropriate clients securities. In fact, the very fact that the appellant has chosen to even raise such an allegation only proves its intentional defiance of the authority of the respondents to regulate the markets and the conduct of the brokers.

64. In fact, one of the guiding principles in interpreting securities laws, rules, regulations, bye-laws, circulars, etc., ought to be to enhance investor protection and to safeguard the securities markets against mischief of misappropriation of investors securities and money. Directing restitution is essential if the public is to have faith in the system.

65. The innocent clients whose securities have been, thus, misused / misappropriated, cannot be deprived of their right to get back their shares. It may be noted that in the case of ***Sardar Amarjit Singh Kalra (dead) by LRS. And Ors. vs. Pramod Gupta (Smt) (Dead) by LRS and Ors. [(2003) 3 SCC 272]*** a 5 Judge Bench of the Hon'ble Supreme Court, *inter-alia*, held that :-

> *" …… As far as possible, courts must always aim to preserve and protect the rights of parties and extend help to enforce them rather than deny relief and thereby render the rights themselves otiose, "ubi jus ibi remedium" (where there is a right, there is a remedy) being a basic principle of jurisprudence. Such a course would be more conducive and better conform to a fair, reasonable and proper administration of justice….."*

66. Thus, we find that the directions in the impugned orders are not barred by any law, rule, regulations, bye-law or circular. We are of the opinion that the Committee has the power for restitution, to reverse the damage wrongfully caused. The appellants having committed a wrongful act cannot be permitted to take advantage of its own wrong. Where restitution can be directed, it would be totally contrary to the cause of justice to deny the same. It would be travesty of justice and totally undermine the regulation of the markets if any intermediary is permitted to misuse / misappropriate client's

securities by selling off the same unilaterally when the concerned investor has no outstanding obligation or liability, and then permitting the intermediary to benefit from the same at the cost of expense of the investors.

67. Without prejudice to the aforesaid, it is submitted that in any event, the appellants cannot deny the power and jurisdiction of this Tribunal which has inherent powers and, therefore, the jurisdiction to make restitution. Rule 21 of the Securities Appellate Tribunal (Procedure) Rules, 2000 states that :-

> *"The Appellate Tribunal may make, such orders or give such directions as may be necessary or expedient to give effect to its orders or to prevent abuse of its process or to secure the ends of justice."*

68. Consequently, this Tribunal even on the basis of its own powers can always direct the restitution of the said shares of the investors / clients by the appellant in the interests of protecting the investors and to secure the ends of justice.

69. The allegation that the show cause notice did not state that it was intended to direct the reinstatement of the clients shares is untenable. The show cause notice clearly charged the appellants for

misuse of clients securities and, therefore, obviously if found guilty, the appellants had to reinstate and return the clients shares. The same is a direct consequence and the appellants cannot claim that it was not aware of the same.

70. The contention that any order for restitution must be contingent on unjust enrichment, is incorrect and misconceived. In fact, by wrongfully selling off the clients shares the appellant did evade the losses which it would otherwise have suffered since it had to complete the pay in obligations of the trading member. In the present case, the restitution directed is on the basis that the concerned clients shares had to be returned to them since their shares had been wrongly sold off.

71. In the light of the aforesaid, we are of the opinion that the impugned orders does not suffer from any error of law. All the appeals fail and are dismissed with no order as to costs.

Justice Tarun Agarwala
Presiding Officer

Ms. Meera Swarup
Technical Member

15.12.2023
PTM

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