CIN: L65920MH1994PLC080618
Email: shareholder.grievances@hdfcbank.com
Website: www.hdfcbank.com

HDFC Bank Limited,
Zenith House,
Opp. Race Course Gate no. 5 & 6,
Keshavrao Khadye Marg,
Mahalaxmi, Mumbai- 400034
Tel.: 022 - 3976 0001/0012

January 22, 2021

BSE Limited
Dept. of Corporate Services
Phiroze Jeejeebhoy Towers,
Dalal Street, Fort,
Mumbai 400 001
Scrip Code: 500180

National Stock Exchange of India Limited
Listing Department
Exchange Plaza
Bandra Kurla Complex
Mumbai 400 051
Symbol: HDFCBANK

Dear Sir / Madam,

Sub: Intimation under Regulation 30 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("'the Regulations") by HDFC Bank Limited ("the Bank")

Pursuant to the Regulations, we hereby inform that the Securities & Exchange Board of India ("SEBI"), vide its Final Order dated January 21, 2021 ("the Order"), has levied a monetary penalty of Rupees One Crore payable by the Bank in terms of Section 15HB of the SEBI Act, in the matter of M/s. BRH Wealth Kreators Limited, for non-compliance with the Interim Order issued by SEBI concerning the said matter.

Further, the Bank has been directed vide the Order to transfer an amount of Rs. 158.68 crore along with interest from October 14, 2019 till date, calculated at the rate of 7% p.a. to an interest bearing Escrow Account in any nationalized bank, by marking a lien in favour of SEBI, until the issue of settlement of clients' securities (clients of the stockbroker) is reconciled.

A copy of the Order is enclosed. The Bank is reviewing the Order for considering future course of action.

Yours Truly,
For HDFC Bank Limited

Santosh Haldankar
Sr. Vice President (Legal) & Company Secretary

Encl.: a/a

WTM/GM/MIRSD/MIRSD_DPIEA/10124/2020–21

SECURITIES AND EXCHANGE BOARD OF INDIA

FINAL ORDER

UNDER SECTIONS 11(1), 11B(1), 11B(2) READ WITH SECTION 15HB OF THE SEBI ACT, 1992 IN THE MATTER OF M/S BRH WEALTH KREATORS LIMITED.

NOTICEE	PAN
HDFC BANK LIMITED	AAACH2702H

1. BACKGROUND

1.1 Securities and Exchange Board of India ("**SEBI**") had issued an *Ex Parte Ad Interim Order* cum Show Cause Notice ("**SCN**") against BRH Wealth Kreators Limited (formerly BMA Wealth Creators Limited) ("**BRH/Stock Broker/BMA**") and certain other entities/Noticees on October 7, 2019 ("**Interim Order**") *inter alia* directing at paragraph 9 therein as under:

i. "BRH Wealth Kreators Limited (formerly BMA Wealth Creators Limited), Shiv Kumar Damani, Anubhav Bhatter, Murgesh Devashrayi, BRH Commodities Private Ltd. (formerly BMA Commodities Pvt. Ltd.), Prosperous Vyapaar Private Limited, Polo-Setco Tie Up Private Limited and Parton Commercial Private Limited are restrained from accessing the securities market and are further prohibited from buying, selling or otherwise dealing in securities, either directly or indirectly, or being associated with the securities market in any manner whatsoever, till further directions;

ii. The aforesaid Noticees shall cease and desist from undertaking any activity in the securities market, directly or indirectly, in any manner whatsoever till further directions;

*iii. The aforesaid Noticees are directed not to dispose of or alienate any assets, whether movable or immovable, or to create or invoke or release any interest or charge in any of such assets except with the prior permission of National Stock Exchange of India Limited ("**NSE**") and BSE;*

iv. The aforesaid Noticees are directed to provide a full inventory of all their assets, whether movable or immovable, or any interest or investment or charge in any of such assets, including details of all their bank accounts, demat accounts and mutual fund investments immediately to NSE and BSE but not later than 5 working days from the date of receipt of this Order;

v. *Till further directions in this regard, the assets of the Noticees shall be utilized only for the purpose of payment of money and/or delivery of securities, as the case may be, to the clients/investors under the supervision of the concerned Exchanges/depositories;*

vi. *The depositories are directed to ensure that no debits are made in the demat accounts, held jointly or severally, of the aforesaid Noticees and persons except for the purpose mentioned in sub–para (v) above, after confirmation from NSE/BSE;*

vii. *The banks are directed to ensure that no debits are made in the bank accounts held jointly or severally by the Noticees except for the purpose of payment of money to the clients/investors under the written confirmation of NSE/BSE;*

viii. *The Exchanges, clearing corporations and depositories shall appoint forensic auditor to track misuse of client's funds/securities and to identify the net assets/liabilities of Noticee no. 1 (BRH Wealth Kreators Limited) and Noticee no. 5 (BRH Commodities Private Ltd.) and submit the report to SEBI within 90 days;*

ix. *The Exchanges shall deal with the complaints/claims of the clients against the member and may return the amount of client fund and securities to the clients and may also use assets of the Noticee no. 1 to meet clients'/Exchanges'/clearing members'/clearing corporations', obligations."*

1.2 Subsequent to the Interim Order, SEBI had received a letter dated November 7, 2019, from HDFC Bank Limited ("**HDFC/Noticee**") *inter alia* submitting as under:

a. *"HDFC has granted credit facilities to BRH & BRH Commodities Pvt. Ltd. ("**BRH Commodities**") (Collectively referred to as "**Borrowers**") aggregating to ₹191.16 Crore & ₹26.61 Crore, respectively.*

b. *HDFC has recalled the credit facilities from the Borrowers and the amounts outstanding under the respective facilities to each of the Borrower is due and payable by the Borrowers to the Bank.*

TABLE I – DETAILS OF CREDIT FACILITIES AVAILED BY BRH FROM HDFC			
	DETAILS OF CREDIT FACILITIES	**BRH PRINCIPAL O/S ON THE DATE OF RECALL I.E. 4.10.2019**	**BRH COMMODITIES PVT. LTD. PRINCIPAL O/S ON THE DATE OF RECALL I.E. 4.10.2019**
		AMOUNT IN ₹ CRORE	
1.	BANK GUARANTEE/STL FACILITY FOR EXCHANGE MARGIN REQUIREMENTS (PARTIALLY SECURED BY LIEN MARKED FIXED DEPOSITS)	34.50	9.50
2.	OD/LOAN AGAINST PROPERTIES	17.57	17.11
3.	OD/LOAN AGAINST SECURITIES	87.75	-
4.	OD AGAINST BOOK DEBTS	50.47	-
5.	OD AGAINST FIXED DEPOSITS	0.24	-
6.	OTHER MISC. TODS AND OUTSTANDING CORPORATE CREDIT CARD DUES	0.63	-
	TOTAL	**191.16**	**26.61**

c. *The facilities mentioned hereinabove for the Borrowers are cross collateralized by way of a right of lien and set off forming part of the loan documents executed by the Borrowers at the time of availing the above facilities. Bank Guarantees ("**BGs**") forming part of the credit facilities mentioned above, have been issued by the Bank in favour of Clearing Corporations/Stock Exchanges. Notwithstanding any defaults being made by the Borrowers under their respective loan documents and/or recall of the credit facilities by the Bank and/or to the relevant clearing corporation/Exchange, the terms of the BGs issued to beneficiaries require the Bank to unconditionally honour the BGs and make payment under the BGs to the beneficiaries.*

d. *We wish to draw your attention to the fact that the monies are due and payable to the Bank by the Borrowers pursuant to loan documents agreements which were executed much before issuance of the (Interim Order) and securities in relation to the respective loan documents were also created by each of the Borrowers much prior to the (Interim Order). Bank is a custodian of public monies and is expected to ensure that the interests of the deposit holders is not jeopardised. To achieve this objective, the Bank is required to enforce and realise the securities furnished by the Borrower to recover outstanding dues including principal and periodic interest. In this regard, we wish to submit that the Bank has credited and shall continue to credit the sales proceeds of the enforced securities in the accounts of the Borrowers and debit the accounts for the following:*

   i. *Payments being made to clearing corporations/Exchanges/beneficiaries upon invocation of BGs issued by the Bank.*

ii. *Recovery of outstanding dues including principal and interest due from the Borrowers against the credit facilities advanced to them as mentioned hereinabove.*

e. *We trust the above is in order and request a line of confirmation that the aforesaid steps taken by the Bank are in compliance with SEBI Orders."*

1.3 In reply to the above–mentioned letter, vide a letter dated December 13, 2019, SEBI while referring to the directions contained in the Interim Order [reproduced at paragraph 1.1(v) – (vii)] informed HDFC as under:

a. *"It is observed from your letter that HDFC had granted OD/Loan against securities for ₹87.75 Crore. However, it is observed from the information provided by NSE that the Bank has invoked securities pledged by BRH to the tune of ₹158.7 Crore as on October 14, 2019. Thus, actions of the Bank are not in conformity with the directions given under the Interim Order."*

1.4 During the intervening period, the directions issued vide the Interim Order were confirmed against BRH and certain other entities/Noticees mentioned therein vide SEBI Order dated January 2, 2020.

1.5 Thereafter, vide a reply dated February 14, 2020, HDFC responded to the above mentioned SEBI letter dated December 13, 2019 *inter alia* stating as under:

a. *"The Bank humbly submits that its actions are in accordance with law ... and thus it would not be correct to state that the same are not in conformity with (the Interim Order), whether for the reasons cited in your letter or otherwise. The Bank's act of invoking the securities provided under the Overdraft ("**OD**")/ Loan against Securities ("**LAS**") facility for amounts higher than the outstanding under the said facility is in accordance with its right of general lien as afforded under Section 171 of the Contract Act, 1872, which right is expressly reserved in the relevant loan documents executed with BRH and BRH Commodities, respectively, as stated in our letter dated November 7, 2019.*

b. *The Bank is thus fully entitled in law to appropriate proceeds from sale of the securities for any outstanding of the concerned Borrowers, whether the securities were provided for that specific facility or not."*

2. SHOW CAUSE NOTICE DATED MARCH 19, 2020:

2.1 The allegations levelled against HDFC in the SCN dated March 19, 2020 ("**SCN**"), are summarised hereunder –

i. **NON–COMPLIANCE WITH THE DIRECTIONS CONTAINED IN THE INTERIM ORDER THROUGH INVOCATION OF PLEDGE OF SECURITIES –** NSE had informed SEBI that BRH had availed *LAS* facility from the Noticee by way of pledging securities from two demat accounts maintained with Central Depository Services (India) Limited ("**CDSL**") and as on September 30, 2019, the total securities pledged from the said accounts were as under:

TABLE II – DETAILS OF SECURITIES PLEDGED BY BRH IN FAVOUR OF HDFC		
BENEFICIAL OWNER ID	***PLEDGED QUANTITY***	***PLEDGED AMOUNT (₹IN CRORE)***
1204630000021137*	1,73,53,289	144.38
1204630000155615	27,17,351	14.30
TOTAL	**2,00,70,640**	**158.68**
****AS PER THE DEPOSITORY RECORDS SUBMITTED BY NSE, THIS DEMAT ACCOUNT WAS TAGGED AS 'CORPORATE CM/TM CLIENT ACCOUNT' WITH THE DEPOSITORY INDICATING THAT THE ACCOUNT WAS MAINTAINED FOR SAFEKEEPING OF SECURITIES RECEIVED FROM CLIENTS OF BRH.***		

ii. HDFC had granted credit facilities to BRH (₹191.16 Crore) and BRH Commodities (₹26.61 Crore), out of which an amount of ₹87.75 Crore was granted as *LAS*. On October 14, 2019, HDFC had invoked securities pledged by BRH to the extent of ₹158.68 Crore. The aforementioned invocation of pledge of client securities available in the aforementioned two demat accounts of BRH, by HDFC, was allegedly not in conformity with the directions contained in the Interim Order.

iii. **VIOLATION OF CLAUSE 2.5 OF ANNEXURE TO SEBI CIRCULAR NO. SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 DATED SEPTEMBER 26, 2016 ("SEPTEMBER 2016 CIRCULAR") READ WITH CLAUSE 2(C) OF SEBI CIRCULAR NO. CIR/HO/MIRSD/MIRSD2/ CIR/P/2017/64 DATED JUNE 22, 2017 ("June 2017 Circular") –** As per the aforementioned Circulars, BRH was permitted to only pledge securities of debit balance clients or clients having indebtedness to BRH at the time of creation of such pledge. It was alleged that as HDFC did not conduct adequate due diligence to verify that securities pledged in its favour actually belonged to clients of BRH having debit balance at the time of creation of pledge, the pledge created on the securities held in BO A/c no. 1204630000021137 was invalid and the subsequent invocation of such pledge by HDFC, was therefore illegal. Had the pledge not

been invoked, the securities belonging to clients would have been available for restitution/settlement of claims of the clients of BRH.

iv. **VIOLATION OF CLAUSE 4.8 OF SEBI CIRCULAR NO. CIR/HO/MIRSD/DOP/CIR/P/2019/75 DATED JUNE 20, 2019 ("June 2019 Circular")** – As per the aforementioned Circular, the client's securities already pledged in terms of the September 2016 and June 2017 Circulars, shall, by August 31, 2019 (extended to September 30, 2019) either be unpledged and returned to the clients upon fulfillment of pay–in obligation or disposed of after giving notice of 5 days to such client. As a professional Clearing Member and Clearing Bank, HDFC was expected to be aware of the aforesaid Circular. However, HDFC had invoked the pledge of securities without giving the requisite notice of 5 days to the clients of BRH thus depriving them of a fair opportunity to claim back their securities. HDFC had allegedly violated Clause 4.8 of the aforementioned Circular.

v. **FAILURE BY THE NOTICEE TO EXERCISE DUE DILIGENCE WHILE EXTENDING CREDIT FACILITIES TO BRH:** The credit availed by BRH through the OD/*LAS* facility was for a principal amount of ₹87.75 Crore. However, HDFC had invoked a pledge of client securities available in the aforementioned two demat accounts of BRH, worth ₹158.68 Crore. Further, as per the unaudited financial accounts as on March 31, 2019 (as submitted by BRH), the networth stood at ₹12.83 Crore against the pledged securities having an aggregate value of ₹169.24 Crore as on September 30, 2019. It is alleged that HDFC had failed to exercise due diligence while extending credit facilities to BRH without verifying the networth vis–a–vis the amount of credit facilities extended.

2.2 As per the SCN, HDFC was directed to show cause as to why suitable directions under Sections 11(1), 11B(1), 11B(2) read with 15HB of the SEBI Act, 1992 ("**SEBI Act**") including but not limited to a direction to return the securities whose pledge was invoked and/or a direction to return to BRH the money so realised from the sale of such pledged securities, should not be issued against HDFC for the alleged violations as stated as paragraph 2.1.

2.3 HDFC had filed a reply dated June 6, 2020, to the SCN, the contents of which are detailed elaborately and dealt with in seriatim at paragraphs 3 and 4 below.

2.4 **PERSONAL HEARING:** Pursuant to the above, an opportunity of personal hearing was granted to the Noticee on September 3, 2020. The Noticee appeared for the hearing and was represented by Advocate Gaurav Joshi, Advocate Bindi Dave, Anantharaman S. and Anand Mankodi from HDFC. The Noticee reiterated the submissions contained in its replies dated June 6, 2020 and September 3, 2020. The Noticee was granted time till September 10, 2020, to file additional written submissions, if any. Accordingly, the Noticee submitted additional written submissions vide letter dated September 10, 2020. The aforementioned replies are also discussed and dealt with at paragraphs 3 and 4 below.

3. *JURISDICTION ISSUE: WHETHER SEBI HAD EXCEEDED ITS JURISDICTION IN ISSUING THE SCN TO THE NOTICEE ALLEGING NON–CONFORMITY WITH THE INTERIM ORDER?*

3.1 As per the SCN, NSE had informed SEBI that BRH had availed *LAS* facility from the Noticee by way of pledging securities from two demat accounts maintained with Central Depository Services (India) Limited ("**CDSL**"), viz. 1204630000021137 and 1204630000155615, and as on September 20, 2019, the total securities pledged from the said accounts amounted to ₹158.68 Crore. HDFC had granted credit facilities to BRH (₹191.16 Crore) and BRH Commodities (₹26.61 Crore), out of which an amount of ₹87.75 Crore was granted as *LAS*. On October 14, 2019, HDFC had invoked securities pledged by BRH to the extent of ₹158.68 Crore. As per the SCN, the aforementioned invocation of pledge of client securities available in the aforementioned two demat accounts of BRH, by HDFC, was alleged to not be in conformity with the directions contained in the Interim Order.

3.2 In response, the Noticee has *inter alia* submitted as under:

a. *SEBI's SCN purportedly issued under Sections 11(1), 11(B)(1), 11(B)(2) read with Section 15HB of the SEBI Act is bereft of jurisdiction and is an instance of regulatory over–reach into the HDFC's regular banking business.*

b. *Through Advocates' email dated September 1, 2020, we had requested SEBI to provide all the documents referred to and relied upon while issuing the SCN and also copies of SEBI's file pertaining to BRH, and/ or all inspection/ inquiry/ investigation reports in relation thereto. SEBI, however, has not provided any of the inspection/ inquiry/ investigation reports in its file and has*

only provided two transaction statements and an excel sheet which shows details of the pledged securities invoked by HDFC purportedly from CDSL's records.

c. *It is also pertinent to note that on 11th June 2020, BRH filed a Suit against HDFC Bank before the Calcutta High Court, being CS No.54 of 2020, praying for a decree of mandatory injunction for return of the securities on which the pledge was invoked by HDFC Bank. Annexed hereto and marked as* ***Annexure 'V'*** *is a copy of the Case Status of as available on the Calcutta High Court website. The matter pertaining to invocation of the pledge of securities is thus clearly sub judice before a Civil Court of competent jurisdiction. The Hon'ble Calcutta High Court is already seized of BRH's Suit for return of the pledged securities or in the alternative, value thereof. The Hon'ble Calcutta High Court, being a higher forum, SEBI ought not to take cognizance of the instant matter till disposal of the proceedings in the said High Court. Additionally, given the facts and circumstances, it may be more appropriate that questions of validity of pledge and invocation thereof be tried by a civil court of competent jurisdiction with evidence being led rather than in the instant summary proceedings. Separately, almost identical issues of law as are arising herein are also sub judice before the SAT in HDFC's Appeal No.70 of 2020 against SEBI's Order dated December 13, 2019 in the matter of Karvy Stock Broking Limited.*

d. *As part of its regular banking business, Noticee has extended various loan facilities to BRH since 2005. Among other loan facilities, Noticee has also extended loans against shares/securities to BRH. The LAS facility extended by Noticee to BRH has been increased and/or renewed from time to time. As is the case with most LAS facilities, the LAS Facility extended to BRH is inter alia secured by way of a pledge of securities created by BRH in favour of Noticee. In or around 2005, BRH, had approached Noticee with a request for an overdraft facility. At the time BRH offered to pledge the subject shares as collateral to the facility and in fact in its Declaration under the Overdraft Request Letter dated October 7, 2005, under para 4 thereof, expressly and unequivocally represented and declared to HDFC inter alia that the securities being pledged were held by BRH in its name as absolute owner thereof and not in any other fiduciary capacity. On the basis of such representations inter alia, which were material inducement for HDFC to disburse the monies under the overdraft facility, HDFC agreed to grant various overdraft facilities, including the LAS Facility, to BRH by and under various Loan Agreements, which were increased and/ or renewed from time to time. HDFC sanctioned an increase of the limit of the overdraft facility, first in 2007 by*

*way of the Loan Agreement dated August 10, 2007 upto an additional limit of ₹50,00,00,000 and then in 2014 under the Loan Agreement dated June 21, 2014 upto a further additional limit of ₹100,00,00,000. Pertinently, BRH made the same Declaration under the Overdraft Request Letters for all the Loan Agreements pertaining to the LAS Facility granted to BRH, viz. that the securities being pledged were held by BRH in its name as absolute owner thereof and not in any other fiduciary capacity. In fact, by and under clause 13 (ii) the Loan Agreement dated June 21, 2014, BRH agreed and confirmed to maintain segregation of securities held by him/ her on behalf of clients from the securities held by BRH in its name. Further, by and under clause 13(iii) of the said Loan Agreement, BRH expressly agreed and confirmed that client securities will not be offered as security for the borrowing in any manner. Additionally, the Loan Agreements, as also other loan documents, including HDFC's Sanction Letter dated December 10, 2018, at clause 15 to Annexure 1 thereof, expressly reserved the Bank's right to a general lien and set off as available to it under law. Pursuant to these covenants, all of the securities pledged by BRH to HDFC in respect of the LAS Facility stood in the name of BRH as beneficial owner ("**BO**") in the records of CDSL as available/ accessible by HDFC. As the shares/ securities offered as collateral stood in the name of BRH as BO thereof as per the records of CDSL, HDFC was fully entitled to accept a pledge of such shares/ securities from BRH under Sections 10 and 12 of the Depositories Act more so in view of BRH's express representations and declarations that the pledged securities were held in its name as absolute owners thereof. Since the shares to be pledged were in dematerialized form, the pledge was created in accordance with the provisions of the Depositories Act and Regulations made thereunder. The modalities for creation of the pledge are also set out in the Byelaws and Business Rules of CDSL, which were presumably adhered to by CDSL while permitting marking of pledge on the securities. Pertinently, none of the said provisions require a third–party lender such as HDFC i.e. the pledgee to carry out any investigation into the antecedent title to the securities that are being pledged. The CDSL, after having the opportunity to carry out necessary inquiries as mandated under law, has recorded the pledge in the name of HDFC from time to time without objection. In fact, CDSL's* ***Pledge Master Report*** *for BRH's client ID "00021137" admittedly reflected BRH's name in the field "Name of Pledgor BO". In view of the aforesaid, there was no reason for HDFC to doubt that BRH was the rightful owner of the securities pledged in its favour and the Bank was under a bona fide belief that BRH was the BO for the purposes of Section 10 of the Depositories Act. Furthermore, and in any event, the Bank*

had conducted the requisite due diligence as required by law and was not required by law to carry out any further investigation.

e. *HDFC had invoked the pledge of securities on October 15, 2019 and thereafter sold most of the said securities and appropriated the sale proceeds towards the outstanding under the various credit facilities advanced by HDFC to BRH. Since HDFC was owed amounts under multiple facilities, the Bank was entitled apply and appropriate proceeds of sale of securities provided under the LAS Facility towards its dues in respect of other facilities. This was in accordance with the Bank's right of general lien and set off as afforded under law, which right is expressly reserved in the relevant loan documents executed with BRH, including at paragraph 15 of the Sanction Letter dated December 10, 2018. HDFC had followed the due procedure, as required by CDSL, while invoking the pledge, and the same was permitted by CDSL. In fact, the CDSL did not even object to the further sale of the pledged securities by HDFC. The aforesaid further bolsters the validity of the invocation of pledge by HDFC and shows that such invocation of pledge and sale was not in contravention of SEBI Circulars or its Order dated October 7, 2019. The SCN alleges that pledge created on securities held in BO account number ending with "21137" is invalid and subsequent invocation illegal since HDFC failed to conduct adequate due diligence to verify that the securities pledged in its favour actually belonged to BRH's clients having debit balance at the time of creation of such a pledge. First and foremost, HDFC had no reason to doubt that the pledged securities belonged to BRH and therefore the question of verifying whether it belonged to clients having a debit balance does not arise. Secondly, as stated above, all of the shares pledged to HDFC stood in the name of BRH who was recorded as the beneficial owner of the shares in the records of CDSL, i.e. the concerned depository and HDFC was fully entitled to accept a pledge of such shares from BRH under Sections 10 and 12 of the Depositories Act. HDFC did not have access to any records which showed the nomenclature of BRH's demat account to be that of a client account. HDFC does not have access to and was not provided with the Transaction Statements which purportedly reflect 'Corporate CM/ TM Client account' which are being relied on by SEBI to allege knowledge on HDFC's part of the fact that BRH pledged its clients' securities. In terms of SEBI's Circular dated 26th September 2016 read with SEBI's Circular dated 22nd June 2017 BRH's demat account was required to be shown as 'name of stock broker – client account' and any demat account not so designated will be deemed to be a proprietary account. Therefore, HDFC was entitled to rely on the depository records which did not show the relevant demat account as a client account. The*

Depositories Act provides that the concerned depository is the "registered owner" of the shares, and the "beneficial owner" is the person whose name is recorded as such with the depository. Under Sections 7 and 8 of Depositories Act, it is the depository alone who has the exclusive right and power to enter the name of the "beneficial owner" in its records. Under Section 10 of the Act, such "beneficial owner" is entitled to all the rights and benefits of the securities held in its name. More particularly, under Section 12 the beneficial owner alone is entitled to create a pledge/hypothecation in respect of such securities. Such pledge is intimated to the depository who then makes entries to this effect in its records. Pertinently, Section 12(3) makes it clear that the entry in the records of a depository "shall be evidence of a pledge..." The manner of creation of the pledge is set out in further detail in regulation 58 of the DP Regulations. When a depository receives an application from the beneficial owner for creation of a pledge, regulation 58 requires the depository to carry out an investigation and approve the pledge. It is after such investigation and approval that the depository enters the pledge in its records. The regime created by the Depositories Act is the bulwark of transactions in respect of dematerialised shares. The Hon'ble Bombay High Court in the case of JRY Investments Private Limited vs. Deccan Leafine Services Ltd. and Ors. has also recognised that dematerialised shares have no individual identity and are in a fungible form, as is statutorily recognised in Section 9 of the Depositories Act. It goes on to hold that the Depositories Act has been enacted "for the purpose of recording accurately the transfers and pledges of shares including those in a dematerialised form". Further, it affirms the view that the Depositories Act is a self-contained code that governs the creation of pledge of dematerialised shares and that "ownership and transfer of shares governed by the Act must be in accordance with the provisions of the Depositories Act". Furthermore, the procedure for creation of pledge was also in accordance with the bye-laws and business rules of CDSL, the concerned depository, particularly bye-law 14. Pertinently, under bye-law 14.2, for the purpose of creation of any pledge of securities, CDSL or a participant shall on the application of the beneficial owner, issue a certificate of holdings to the beneficial owner, certifying that the beneficial owner is entitled in its name to securities sought to be pledged. Further, under Bye-law 14.4, CDSL has the power to refuse permission to create a pledge if the same is restrained by virtue of any order or direction of the SEBI. However, it is pertinent to note that NSE and CDSL who were responsible for monitoring utilisation of client collateral by brokers under the extant SEBI Circulars, at no point objected to the creation of pledges by BRH in favour of HDFC. On the contrary, even after publication of June 2019 Circular, the said intermediaries have permitted BRH to create pledges over

securities available in its demat account. In fact, NSE and CDSL have permitted creation of pledges as late as September 27, 2019 without objection. In fact, not only did CDSL, who was covered by SEBI's Circulars and the Interim Order, record the pledge in favour of HDFC but allowed it to invoke the said pledge after the Interim Order and even sell the pledged securities further. The aforesaid clearly shows that the pledge was validly created and invocation of such pledge was not in contravention of Interim Order.

f. *Without prejudice to the aforesaid, and even assuming, without admitting, that the pledged securities belonged to BRH's clients, given that it had pledged the securities in its capacity as a mercantile agent i.e. a stock broker, while acting in the ordinary course of its business and, at the time of creation of pledge, HDFC acted in good faith and was not informed that the pledged securities were purportedly not legally owned by BRH nor that BRH did not have the authority to pledge the said securities, the pledge created in favour of the Bank remains valid and subsisting as per the provisions of Section 178 of the Contract Act, 1872. A stockbroker is therefore a "mercantile agent" under Section 2(9) of the Sale of Goods Act, 1930. Although, SEBI, in its Order dated 13th December 2019 in Karvy's matter, holds in the context of the aforesaid argument relying on Section 178 of the Contract Act that the stock broker is merely a facilitator for placing of buy and sell orders with the stock Exchange and since it did not have any instructions from the clients to buy/ sell securities warranting any movement of securities from accounts of the clients, the "analogy drawn with mercantile agent is wholly misplaced". It is humbly submitted that, even as per the SEBI's own description of the business of a stock broker at paragraph 14(a) of the Order dated December 13, 2019, the same fits the definition of mercantile agent under Section 2(9) of the Sale of Goods Act, 1930. Additionally, the status of the mercantile agent cannot be premised on whether or not the pledge was created validly and in fact the whole Section provides for a situation where the mercantile agent does not have the authority to create the pledge. SEBI, in the aforesaid order, further holds that another reason that Section 178 was not applicable in Karvy's case is because there was an absence of good faith since the lenders allegedly had/ ought to have had notice that Karvy did not have the authority to pledge. While denying the aforesaid conclusion, it is submitted that in any event the said observation does not apply in the instant case as HDFC had acted on good faith on BRH's representations and the Depository's records as accessible to HDFC and without notice that BRH allegedly did not have authority to pledge the concerned securities as is evident from all that is set out hereinabove.*

g. *HDFC is entitled to appropriate the securities provided by BRH towards the LAS Facility for dues under other facilities provided to BRH under the law of mercantile system or the Law Merchant as has been recognised in various judicial pronouncements. It is settled law that under mercantile custom, as also enshrined in Section 171 of the Contract Act, 1872, a bank has a general lien over all forms of securities, except in cases where the deposit was for a particular purpose or where the agreement or contract is inconsistent with the lien. In the instant case, HDFC's right to general lien is reserved in the loan documents as has been set out hereinabove. A banker's general lien over securities received from a customer in the ordinary course of business entitles the bank to use the proceeds from such securities and set it off against any balance that may be due from the customer by way of reduction of the customer's debit balance.*

h. *SEBI, in its SCN, contends that had the pledge not been invoked the securities purportedly belonging to the clients would have been available for restitution/ resettlement of the claims of BRH's clients. The Byelaws of an exchange are a statutory contract between the broker and its client recognised by section 9 of the Securities Contracts (Regulation) Act, 1956 ("**SCRA**"). They cannot be superseded by SEBI except by following the procedure set out in Section 10 of the SCRA. Once arbitration has been incorporated into the Byelaws of NSE and the same have been accepted by the clients of a broker, Section 8 of the Arbitration and Conciliation Act, 1996 mandates that all disputes covered by the arbitration agreement are mandatorily required to be determined by arbitration and no other judicial authority has any jurisdiction to determine such matters. This requirement has been reaffirmed by the Supreme Court on numerous occasions including in the case of **A. Ayyasamy vs. A. Paramasivam & Ors** wherein it was held as follows: "Once there is an arbitration agreement between the parties, a judicial authority before whom an action is brought covering the subject matter of the arbitration agreement is under a positive obligation to refer parties to arbitration by enforcing the terms of the contract. There is no element of discretion left in the court or judicial authority to obviate the legislative mandate of compelling parties to seek recourse to arbitration." In fact, SEBI has already stated in its Order dated January 2, 2020 that claims of investors have to be decided as per the bye-laws of the Exchange.*

i. *Separately, it bears emphasizing that the SCN is purportedly issued on the footing that HDFC's alleged illegal and invalid invocation and sale of the pledged securities has*

prevented settlement or restitution of BRH's clients' claims. However, SEBI itself at paragraph 12 of its Confirmatory Order dated 2nd January 2020 records that a determination of clients' dues has to be completed by conducting a forensic audit and after such determination the stock exchanges and clearing corporations shall take appropriate steps for meeting and realizing investor/ clients' claims. Furthermore, at paragraph 13 of the said Order, SEBI directs that the clients' claims shall be disposed of as per the bye laws of the stock exchanges/ depositories. Therefore, till investors file claims with the exchange and the arbitration is completed as per NSE bye-laws and execution as per byelaws commences, no question of bank having to pay up arises, if at all. More so, when there is no forensic audit itself which determines what the client claims are, if at all.

j. *Furthermore, such a course of action would effectively end up absolving BRH of its liability, who may be the main culprit, if it is found that it pledged client securities. Since, if BRH's clients' dues are recovered from HDFC, there will no longer be any dues owed by BRH to its clients. Even otherwise, for SEBI to pass an order for recovering securities/ sale proceeds from HDFC on the ground that those purportedly belong to BRH's clients, SEBI will have to first make a determination of the clients and their identity and whether or not they are BRH's related parties/ associates/ cronies or high networth individuals and additionally a determination of who, between HDFC and the purported clients are more culpable – a banking company who has followed all due procedures or purported clients who have for years and years not complained or brought to notice any misappropriation of its securities by BRH, since some of the pledges date as far back as 2007.*

k. *Assuming without conceding that the records of CDSL did not correctly record the name of the beneficial owner of the shares in question, the remedy for such a situation is provided in Section 59 of the Companies Act that is referred to above. The NCLT has the power to direct a depository such as CDSL to rectify the name of the beneficial owner, after giving a formal hearing to the parties. In fact, if a transfer of shares takes place in contravention of any special law such as the SEBI Act, then Section 59(4) gives SEBI or the depository the power to approach the NCLT to seek rectification of the records of the depository. It is also pertinent to notice the provisions of Section 59(3), which clarify that until such direction is passed by the NCLT, the holder of the securities is recognised as its owner and continues to have the right to transfer such securities.*

3.3 Before getting into the merits of SEBI's jurisdiction, I would like to trace out the chronological order of events leading to invocation of securities by the Noticee:

A. On **September 30, 2019**, NSE had issued a suspension notice to BRH *inter alia* suspending it as a member with effect from October 1, 2019 for non–compliance of regulatory provisions of the Exchange.

B. Vide a letter dated **September 30, 2019** having subject matter: *"Releasing of client shares"* (a copy of which was marked to SEBI, NSE and BSE), BRH had informed HDFC as under:

"This refers to the credit facility provided by (HDFC) to us. You are aware that by the June 2019 Circular, all stock brokers including us have been directed to segregate securities of their clients. You are also aware that the shares over which you have created pledged against our said credit facility are freely tradable shares and securities of our clients for which full amounts have been paid by the respective clients. You were always aware of such fact and while carrying due diligence this was brought to your notice; however, you still impressed upon us to create the pledge. Though such pledge ought not to have been created in the first place, however, even if created, such pledge is void under SEBI Guidelines. You have also derived benefit from the sale of such shares in the past few months to reduce your credit exposure towards us, which also you should not have done. You cannot dispute that our intention was never to avoid repayment of credit facility and we are committed towards the same. It is in this regard, we had also engaged the services of a world renowned Wealth Management Company namely Alpen Capital (ME) Limited to arrange for alternative source of funding, which would have ensured clearing of our credit facility with you in due course. ... As was informed to you, Alpen is constantly working on unlocking values of real estates, which we have offered to them to arrange the funding. However, none of our efforts can be at the cost of investors' securities or to circumvent their rights. In order to demonstrate our further bona fide intent, we propose to arrange additional collateral securities of equivalent value for you so as to protect the interest of the bank; however, the same can be only done once you release the pledge over the shares of our clients."

C. Vide a letter dated **September 30, 2019**, BRH had also informed NSE (a copy of which was marked to SEBI and HDFC) as under:

"HDFC, JM Financial Ltd. and Bajaj Finance Ltd., who have lent and advance loan facilities to us, have been requested to release all pledge on shares of the clients/customers as those we believe belong to the Clients/Customers and should be transferred to their respective accounts.

Please appreciate that in terms of the June 2019 Circular, we have been constantly working to protect our Clients' funds and securities and have been thriving to segregate shares/securities of our clients. Please note that we are member of CDSL and the shares of the clients held in our custody therein are fully secured. … The issue of creation of pledge is well within your knowledge for long and whether those banks and NBFC should have done the same or not was not within our control. Nonetheless, as stated above, we have requested HDFC, JM Financial Ltd. and Bajaj Finance Ltd. to take other collateral securities and release the pledge forthwith. You would also appreciate that the practice of banks and NBFCs creating pledge over securities have been an age old practice beyond our control and the sudden change brought into effect by the aforesaid Circular issued by SEBI is taking time to take alternate remedial measures. We strongly believe that the interest of the Clients is paramount and in order to protect the same, we are taking and shall continue to take all possible steps to ensure the same.

In these premises, in order to demonstrate our bona fide intention, we hereby request you that if you deem it proper, you may kindly freeze our accounts (1204630000021137, 1204630000023100, 1204630000023115, 1204630000155615, IN30379410000029, IN30379410000037) for the time being in order to protect the interest of Clients/Customers."

D. In its reply to BRH's letter dated **September 30, 2019**, the Noticee vide an e–mail dated October 1, 2019, had requested BRH to fully collateralise its current exposure with the bank under the (i) BG/STL facility – ₹32.50 Crore and (ii) CC/OD (against book debts) – ₹50 Crore and had also informed BRH to repay/pre–pay/reduce its outstanding under LAP/OD against Property (current o/s ₹14.90 Crore), *LAS* (current o/s ₹87.25 Crore) and CC/OD (against book debts) – ₹50 Crore consistent with the present level of business activity.

E. Subsequently, vide a Notice dated **October 4, 2019**, HDFC had recalled the credit facilities granted to BRH aggregating to ₹191.16 Crore (see Table 1) *inter alia* on the grounds that:

(i) NSE had suspended BRH's operations w.e.f. October 1, 2019, and as a consequence of the suspension/cessation of its business, BRH's ability to service the facilities including under the Loan Agreements dated October 7, 2005 ("**1st Loan Agreement**"), August 10, 2007 ("**2nd Loan Agreement**") and June 21, 2014 ("**3rd Loan Agreement**"), stood jeopardised.

(ii) Since the pledged shares were/are lying in the demat accounts with Customer IDs *1204630000021137* and *1204630000155615* under the DP name *'BRH Wealth Kreators Ltd.'* with *'BRH Wealth Kreators Ltd.'* being shown as the BO thereof, there was/is no reason for the Bank to suspect otherwise.

(iii) BRH was trying to misuse the June 2019 Circular to wriggle out of its obligations to HDFC.

F. On **October 7, 2019**, SEBI had issued its Interim Order against BRH and certain other entities/Noticees mentioned therein. As per the Interim Order, BRH was *prima facie* alleged to have:

(i) Failed to segregate securities/monies of clients.

(ii) Furnished misleading information to the exchange regarding shortfall in the value of clients' securities to the tune of ₹93.31 Crores.

(iii) Failed to provide information to NSE regarding client–wise details of securities pledged to NBFCs/Banks/CCs/CM, Register of securities (ROS) for all the registered clients.

(iv) Had failed to unpledge and return the securities to the clients upon fulfilment of pay–in obligation and

(v) Made unauthorised transfer of shares from the clients' demat accounts.

Accordingly, SEBI directed BRH (and certain other entities/Noticees mentioned therein) to immediately cease and desist from undertaking any activity in the securities market and also prohibited it from disposing of or alienating any assets except with prior permission of NSE and BSE. Further, SEBI directed that the assets of BRH shall be utilized only for the purpose of payment of money and/or delivery of securities to the clients/investors under the supervision of the concerned exchanges/depositories.

G. Vide an e–mail dated **October 8, 2019**, BRH had informed HDFC that it would deal with HDFC's letter dated October 4, 2019, within 7 days from October 10, 2019 (being the date of regular operations resuming in BRH's office, after the puja vacations).

H. HDFC replied to BRH vide an e–mail dated **October 9, 2019**, stating that it was entitled to and shall exercise all rights and remedies available to it under the Sanction Letters, Loan Agreements and under the law as per the timelines specified therein.

I. On **October 11, 2019**, HDFC had obtained an independent '*legal opinion*' on the matter stating that in the facts of the instant case the Bank was legally justified, entitled to and free to enforce its rights against securities pledged by BRH.

J. Subsequently, on **October 14, 2019**, HDFC invoked the pledge of securities to the extent of ₹158.68 Crore and thereafter, sold most of the said securities and appropriated the sale proceeds towards the outstanding under the various credit facilities advanced by HDFC to BRH.

3.4 The instant proceedings have essentially arisen on account of non–conformity by the Noticee with the directions contained in the Interim Order issued by SEBI against BRH. The rest of the allegations are off–shoots of the main issue of non–compliance by the Noticee with the Interim Order. The relevant directions as contained at paragraph 9 of the Interim Order are reproduced hereunder:

ii. "The aforesaid Noticees shall cease and desist from undertaking any activity in the securities market, directly or indirectly, in any manner whatsoever till further directions;

iii. The aforesaid Noticees are directed not to dispose of or alienate any assets, whether movable or immovable, or to create or invoke or release any interest or charge in any of such assets except with the prior permission of NSE and BSE;

iv. The aforesaid Noticees are directed to provide a full inventory of all their assets, whether movable or immovable, or any interest or investment or charge in any of such assets, including details of all their bank accounts, demat accounts and mutual fund investments immediately to NSE and BSE but not later than 5 working days from the date of receipt of this Order;

v. ***Till further directions in this regard, the assets of the Noticees shall be utilized only for the purpose of payment of money and/or delivery of securities, as the case may be, to the clients/investors under the supervision of the concerned Exchanges/depositories;***

vi. ***The depositories are directed to ensure that no debits are made in the demat accounts, held jointly or severally, of the aforesaid Noticees and persons except for the purpose mentioned in sub–para (v) above, after confirmation from NSE/BSE;***

vii. ***The banks are directed to ensure that no debits are made in the bank accounts held jointly or severally by the Noticees except for the purpose of payment of money to the clients/investors under the written confirmation of NSE/BSE;"***

3.5 In light of the above mentioned directions, the question is whether the Noticee could have avoided the Interim Order and gone ahead with the invocation of the pledge of securities against the pledgor Stock Broker.

3.6 In the Interim Order, SEBI had *inter alia* directed that BRH shall cease and desist from undertaking any activity in the securities market and further, its assets shall be utilised only for the purpose of payment of money and/or delivery of securities, as the case may be, to the clients or investors under the supervision of the concerned Exchanges or Depositories. As such, the expression *"assets of the Noticees"* at paragraph 9(v) of the Interim Order (reproduced at paragraph 3.4) would extend to all properties of BRH including securities that were pledged by it against which funds were raised from the Noticee, Bajaj Finance Limited and JM Financial Products Limited. It is pertinent to note that the Interim Order had quantified the outstanding loans of the Noticee at paragraph 7F therein. When a loan outstanding of a broker is adjusted against the pledged securities belonging to its clients, it is the broker which gets benefitted as it reduces its liability. Such a reduction of the broker's liability is at the cost of its clients. It is relevant to emphasise that the underlying object of the Interim Order was to protect the securities belonging to the clients and in case of shortfall, to utilise other assets of the Stock Broker to meet claims of its clients. Thus, the impact of the Interim Order was to impose an immediate freeze *inter alia* on the assets of the Stock Broker, in whatever form it was and wherever it was situated irrespective of who was in possession of such assets. Further, vide the directions at paragraphs 9(vi) and 9(vii) of the Interim Order, the depositories and banks were directed not to make debits from the demat accounts/bank accounts of BRH.

3.7 In this connection, it is relevant to mention that the Interim Order as issued by SEBI invoking powers under Sections 11(1), 11(4), 11B and 11D of the SEBI Act partakes the character of *'an order in rem'* and binds all constituents dealing with the broker or his assets/liabilities till the completion of the investigation/forensic audit. Such interim freezing orders cannot be stated to be binding only on the person/entity which has contravened the provisions of securities laws but also binds other constituents in the market such as banks, companies, intermediaries, etc. who have dealt with the subject assets of the Stock Broker or entered into transactions with the said broker or its clients. The Noticee, by invoking the securities pledged by the Stock Broker, which were frozen vide the Interim Order, has "dealt in securities" which were specifically frozen for a stipulated time.

3.8 It is a settled legal position that even if an order is void, it requires to be so declared by a competent forum and it is not permissible for any person to ignore the same merely because in his opinion the order is void. In the matter of ***Pune Municipal Corporation vs. State of Maharashtra & Ors, Appeal (Civil) 1084 of 2006 – Date of judgment: February 26, 2007,*** the Hon'ble Supreme Court had an occasion to consider a similar question. The Division Bench of the Bombay High Court had set aside an order passed by the Additional Collector and Competent Authority, Pune in 1977, on the ground that no notice was served on the owners before declaring their land to be excess and vacant land under Section 8 of the Urban Land (Ceiling & Regulation) Act, 1976. Pune Municipal Corporation had challenged the Bombay High Court's order before the Hon'ble Supreme Court. The order of the Additional Collector was set aside by the Revisional Authority in 1990 in a different context without hearing the Corporation. The Bombay High Court upheld the order of the Revisional Authority, without hearing the Additional Collector or the Corporation as it held that the Corporation was not an 'affected' party. In this context, the Hon'ble Supreme Court made some relevant observations, while upholding the original order passed by the Additional Collector, Pune and setting aside the order passed by the Bombay High Court confirming the order of the Revisional Authority. Such observations are extracted below:

"It is well settled that that no order passed by the competent authority can be ignored altogether unless a finding is recorded that it was illegal, void or not in consonance with law. As Prof. Wade states: "The principle must be equally true even where the 'brand of invalidity' is plainly visible; for there also the order can effectively be resisted in law only by obtaining the decision of the Court".

He further states:

"The truth of the matter is that the court will invalidate an order only if the right remedy is sought by the right person in the right proceedings and circumstances. The order may be hypothetically a nullity, but the Court may refuse to quash it because of the plaintiff's lack of standing, because he does not deserve a discretionary remedy, because he has waived his rights, or for some other legal reason. In any such case the 'void' order remains effective and is, in reality, valid. It follows that an order may be void for one purpose and valid for another, and that it may be void against one person but valid against another".

*In **Smith vs. East Elloe Rural District Council, 1956 AC 736 at 769: (1956) 1 All ER 855**, Lord Redeliffe had an occasion to consider a similar argument (that the order was null and void). Negativing the contention, the Law Lord made the following off-quoted observations: "(T)his argument is in reality a play on the meaning of the word 'nullity'. An order even if not made in good faith, is still an act capable of legal consequences. It bears no brand of invalidity upon its forehead. Unless the necessary proceedings are taken at law to establish the cause of invalidity and to get it quashed or otherwise upset, it will remain as effective for its ostensible purpose as the most impeccable of orders" (emphasis supplied).*

3.9 In another matter, ***Krishnadevi Malchand Kamathia and Ors vs. Bombay Environmental Action Group and Ors., Civil Appeal No. 4421 of 2010 before the Supreme Court of India – Date of judgment: January 31, 2011,*** the question before the Hon'ble Supreme Court was whether the appellants could have defied the Orders passed by the District Collector under the Indian Forest Act 1927 and Forest (Conservation) Act, 1980, on the ground that a Notification which was the basis of such Orders, was alleged to be void *ab initio* by the appellant therein. Allegedly, as per the appellants, the Notification did not disclose the statutory provisions which conferred the power/competence upon the District Collector to issue the said Notification. In this context, the Hon'ble Supreme Court had observed:

*"18. In **State of Kerala vs. M.K. Kunhikannan Nambiar Manjeri Manikoth Naduvil (dead) & Ors., AIR 1996 SC 906; Tayabbhai M. Bagasarwalla & Anr. vs. Hind Rubber Industries Pvt. Ltd. etc., AIR 1997 SC 1240; M. Meenakshi & Ors. vs. Metadin Agarwal (dead) by L.Rs. & Ors. (2006) 7 SCC 470; and Sneh Gupta vs. Devi Sarup & Ors., (2009) 6 SCC 194**, this Court held that whether an order is valid or void, cannot be determined by the parties. For setting aside such an order, even if void, the party has to approach the appropriate forum.*

*19. In **State of Punjab & Ors. vs. Gurdev Singh, Ashok Kumar, AIR 1991 SC 2219**, this Court held that a party aggrieved by the invalidity of an order has to approach the court for relief of*

declaration that the order against him is inoperative and therefore, not binding upon him. While deciding the said case, this Court placed reliance upon the judgment in Smith vs. East Ellore Rural District Council, [1956] 1 All ER 855 ...

*20. In **Sultan Sadik vs. Sanjay Raj Subba & Ors., AIR 2004 SC 1377**, this Court took a similar view observing that once an order is declared non–est by the Court only then the judgment of nullity would operate erga omnes i.e. for and against everyone concerned. Such a declaration is permissible if the court comes to the conclusion that the author of the order lacks inherent jurisdiction/competence and therefore, it comes to the conclusion that the order suffers from patent and latent invalidity.*

21. Thus, from the above it emerges that even if the order/notification is void/voidable, the party aggrieved by the same cannot decide that the said order/notification is not binding upon it. It has to approach the court for seeking such declaration. The order may be hypothetically a nullity and even if its invalidity is challenged before the court in a given circumstance, the court may refuse to quash the same on various grounds including the standing of the petitioner or on the ground of delay or on the doctrine of waiver or any other legal reason. The order may be void for one purpose or for one person, it may not be so for another purpose or another person."

3.10 Thus, the act of invocation of the pledge by the Noticee avoiding the Interim Order without paying deference to the restrictions imposed on the assets of the Stock Broker, is against the settled position in law, as brought out above. If the Noticee's right to recover its dues from BRH was affected on account of the Interim Order, it could have approached a Court/Forum of competent jurisdiction before such conscious avoidance of the said Order. The right to challenge such orders by an "affected party" in an appropriate forum is always available under the statute. In any case, the Noticee could not have unilaterally chosen to ignore the directions contained in the Order of a Regulator and proceed with its recovery, claiming to have been guided by an independent '*legal opinion*'.

3.11 I have also perused the *'legal opinion'*, the relevant extracts of which are reproduced below:

"As far as the Order dated 7th October 2019 is concerned, significantly the Querist (HDFC) is neither made a party nor was any notice issued to the Querist. There is a general order stating that the banks should ensure that no debits are made in the bank accounts held jointly or severally by the "Noticee" i.e. BMA. There is no direction whatsoever in the order of SEBI which

restrains the Querist from exercising in any manner the Querist's right of enforcement for the securities.

In the premise, therefore, I am of the opinion that the Querist is legally justified, entitled to and free to enforce its rights against the pledged securities in accordance with law. The Querist would be legally justified in enforcing the pledged shares to recover the outstanding amounts which are due to the Querist.

The Order of SEBI dated 7th October 2019 merely provides that the banks shall not make any debits in the bank accounts held by BMA as specified therein. In my opinion, the Querist may appropriate the proceeds as long as they are not deposited in any bank account of BMA held jointly or severally with the Querist."

3.12 As brought out in the preceding paragraphs, one of the objectives sought to be achieved by the Interim Order was the protection of client securities. The directions at paragraphs 9(ii)–(v) of the Interim Order (reproduced at paragraph 3.4) therefore, have to be read holistically. Paragraph 9(vii) of the Interim Order (reproduced at paragraph 3.4) was a generic direction given to the banks not to debit bank accounts held by BRH except for the purpose of payment of money to clients/investors under written confirmation of NSE/BSE. The Noticee does not qualify to fall within the general category of banks contemplated under the aforementioned paragraph 9(vii) of the Interim Order since it had advanced huge loans to BRH for broking business. The Noticee was made aware that BRH had utilised/misappropriated its clients' securities for various purposes including raising of loans/funds, vide the Interim Order. The question of whether the Noticee could have invoked the pledge of securities has to be considered in light of the whole set of facts brought out in the Interim Order. A perusal of the *'legal opinion'* shows that it has only taken into consideration the issue of whether the directions at paragraph 9(vii) of the Interim Order are binding on the Noticee or not. In other words, the *'legal opinion'* has segregated and severed the directions at paragraph 9(vii) of the Interim Order from the related operative part of the Interim Order, i.e. the directions at paragraphs 9(ii)–(v) therein. It is reiterated that the directions at paragraphs 9(ii)–(v) of the Interim Order explicitly brought out the underlying objective of the Interim Order. The *'legal opinion'* also tries to justify the invocation of securities pledged by BRH by relying on certain representations and declarations furnished by the Stock Broker at the time of creation of pledge that the pledged securities were held in its name as absolute owner thereof. In this regard, even if it were to be accepted that BRH was the absolute owner of the securities pledged with the Noticee, the invocation by the Noticee would still not have been permissible in view of the aforementioned directions of the Interim Order. Therefore,

in my opinion, the reliance placed by the Noticee on the *'legal opinion'* for invocation of securities pledged by BRH, is misplaced and incorrect. Further, the Interim Order was a speaking Order which brought out the context that compelled SEBI to issue the ex–parte directions (see paragraph 3.3.F). Hence, the avoidance of the Interim Order by the Noticee will make it liable under the securities laws.

3.13 The intent and the spirit of SEBI's action together with the mandate of SEBI's powers flowing from the statute was captured in the Interim Order. The intent of the Interim Order was to protect the interest of the investors/clients of BRH through an immediate freeze of the "*assets of the Noticees*", etc. and also for ensuring that BRH ceases and desists from undertaking any activity in the securities market. Further, the Interim Order was not an ultimate determination of the rights of recovery of the Noticee but rather intended to ensure a freeze on the assets of BRH until completion of the investigation/forensic audit and that the investors' interests are not compromised in any manner whatsoever. Having regard to the aforementioned, the Noticee cannot now contend that the directions contained in the Interim Order, including restraining BRH from disposing of its assets for any purpose other than payment of client funds and securities, were not binding on it. Having regard to the discussions in the preceding paragraphs, I am of the considered view that the Noticee had consciously invoked the securities pledged by BRH, thereby defeating the directions contained at paragraph 9 of the Interim Order (reproduced at paragraph 3.4).

3.14 As regards the Noticee's submission on insufficiency of documents, in my opinion, the same is one amongst several grounds taken by the Noticee to side step the brazen violation of the directions contained in the Interim Order. The contention raised by the Noticee regarding misrepresentation by BRH at the time of creation of the pledge are all matters of the past and immaterial for the purpose of the instant proceedings. In any view, post the passing of the Interim Order, even a valid creation of pledge will not justify the invocation of securities by the Noticee having regard to the specific directions therein. Realisation of the entire loans outstanding of BRH by the Noticee through invocation of securities that were covered under the Interim Order, tantamounts to an *ex–facie* defiance of the directions passed by an authority established under law. The absence of an order specifically against the Noticee cannot constitute an excuse or a justification for the aggressive recovery measures adopted by the Noticee, after it having become aware of the Interim Order.

4. *MISCELLANEOUS ISSUES:*

4.1 The SCN has alleged violation of Clause 2.5 of the September 2016 Circular and Clause 2.c. of the June 2017 Circular as well as violation of the June 2019 Circular. Additionally, the SCN has also alleged that HDFC had failed to conduct adequate due diligence to verify that securities pledged by BRH actually belonged to clients (of the said Broker) having debit balance at the time of creation of pledge.

4.2 In its submissions, the Noticee has mainly questioned the maintainability of the aforementioned allegations against it as the SEBI Circulars were directed towards intermediaries registered with SEBI like recognized stock exchanges, clearing corporations, depositories, trading members/ clearing members and/ or depository participants and not to third party lenders. Further, merely because the Noticee was a clearing member, it did not make it liable for the alleged violations. The Noticee has also contended that the lending activity and clearing activity were done by separate departments. The Noticee has contended that it is governed by RBI and its guidelines and Circulars while granting loans and advances. In fact, RBI Circulars/guidelines regarding loans and advances expressly permit banks to grant working capital facilities to stock–brokers registered with SEBI. Separately, for creation of pledge over shares/securities, the Noticee follows the modalities for creation as set out in the Depositories Act, Regulations framed thereunder and the Bye–laws and Business Rules of the concerned Depository.

4.3 As noted from the observations in paragraphs 3.3 to 3.14 above, the Noticee could not have unilaterally chosen to ignore the directions contained in the Interim Order prior to proceeding with its recovery on the claim that it was guided by the '*legal opinion.*' Further, the Noticee has not approached a Court/Forum of competent jurisdiction prior to avoidance of the Interim Order through invocation of securities pledged by BRH. In my view, the aforementioned act of the Noticee is the main cause for concern in the instant proceedings. Given the unilateral action of the Noticee to avoid SEBI's Interim Order, I am of the view that the alleged violations of SEBI Circulars as also the failure to conduct due diligence by the Noticee to verify the ownership of securities pledged at the time of creation of the pledge, are not relevant for consideration at this point in time. As stated earlier, the validity of the pledge at the time of creation does not justify the subsequent act of invocation by the Noticee on October 14, 2019, post the Interim Order. Further, I also note that the issue of validity of pledge and invocation thereof is pending

determination by the Hon'ble Calcutta High Court, as pointed out by the Noticee. At this stage, I do not intend to get into the merits of the aforementioned allegations in the SCN.

4.4 Thus, to conclude, I find the invocation of pledge of client securities available in the two demat accounts of BRH (having beneficial owner ID nos. 1204630000021137 and 1204630000155615), by the Noticee, was not in conformity with the directions contained in the Interim Order. I find that the Noticee had unilaterally invoked securities pledged by BRH to the extent of ₹158.68 Crore. I am therefore, of the considered view that the Noticee be directed to deposit an equivalent amount of ₹158.68 Crore along with interest from October 14, 2019 till date, at the rate of 7% per annum (being the Marginal Cost of Funds based Lending Rate (MCLR) notified by the RBI) in a separate interest bearing Escrow Account, till the issue of settlement of clients' securities is reconciled.

4.5 I note that the SCN in the present matter has also been issued under Section 11B (2) and Section 15HB of the SEBI Act. I note that the power given under Section 11B (2) is without prejudice to the power to issue directions under Sections 11(1) and 11B(1) of the SEBI Act. Section 15HB of SEBI Act provides as under:

"Penalty for contravention where no separate penalty has been provided.

15HB. Whoever fails to comply with any provision of this Act, the rules or the regulations made or directions issued by the Board thereunder for which no separate penalty has been provided, shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one Crore rupees."

4.6 Having regard to the facts and circumstances in the instant proceedings, including the fact that the Noticee had consciously proceeded to defeat the directions in the Interim Order, I am of the considered view that in terms of Section 15HB of the SEBI Act, a penalty of ₹ One Crore be imposed on the Noticee for non–compliance with the Interim Order.

DIRECTIONS

5.1 In view of the foregoing, I, in exercise of the powers conferred upon me under Section 19 read with Sections 11(1), 11B(1), 11B(2) read with Section 15HB of the SEBI Act and in the interest of investors and the securities market, hereby direct as under:

i. HDFC (PAN: AAACH2702H) is directed to transfer an amount of ₹158.68 Crore along with interest from October 14, 2019 till date, calculated at the rate of 7% per annum to an interest bearing Escrow Account ["**Escrow Account in Compliance with SEBI Order dated January 21, 2021 – A/c (in the name of the respective Noticee)**"], in any Nationalized Bank, by marking a lien in favour of SEBI, until the issue of settlement of clients' securities is reconciled.

ii. HDFC shall be liable to a monetary penalty of ₹ **One Crore** which shall be payable within a period of forty–five (45) days, from the date of this Order, by way of demand draft in favour of *"SEBI–Penalties remittable to Government of India"*, payable at Mumbai, or by online payment through following path on the SEBI website: www.sebi.gov.in/ENFORCEMENT → Orders → Orders of Chairman / Members → Click on PAY NOW or at the link https://siportal.sebi.gov.in/intermediary/AOPaymentGateway.html.

iii. HDFC shall forward details of the demand draft or online payment made (in the format as given in the table below) to the "*The Division Chief, Market Intermediaries Regulation and Supervision Department – Division of Post Inspection Enforcement Action, Securities and Exchange Board of India, SEBI Bhavan, Plot no. C-4A, 'G' Block, Bandra Kurla Complex, Bandra (E), Mumbai–400051*". HDFC shall provide the following details while forwarding the demand draft/payment information:

Case Name:	
Name of Payee:	
Date of Payment:	
Amount Paid:	
Transaction No.:	
Bank Details in which payment is made:	
Payment is made for:	*Penalty*

iv. HDFC shall keep the Reserve Bank of India informed about this Order, within a week from the date of receipt of Order.

v. HDFC shall ensure to place a copy of this Order before its Board.

vi. HDFC shall immediately make a disclosure of this Order on its website for public dissemination.

5.2 This Order shall come into force with immediate effect.

5.3 A copy of this Order shall be served upon the recognized Stock Exchanges, Depositories, Registrar and Transfer Agent(s) of Mutual Funds and Banks for necessary compliance.

Place: Mumbai
Date: January 21, 2021

G. MAHALINGAM
WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA