BEFORE THE SECURITIES APPELLATE TRIBUNAL

MUMBAI

In the matter of:

Appeal No.52/2001

Anand Rathi **Appellant**

Vs.

Securities & Exchange Board of India **Respondent**

Appeal No.53/2001

Anand Rathi Securities Pvt.Ltd **Appellant**

Vs.

Securities & Exchange Board of India **Respondent**

Appeal No.54/2001

Anand Rathi Direct (India) Pvt.Ltd **Appellant**

Vs.

Securities and Exchange Board of India **Respondent**

APPEARANCE:

Mr. Aspi Chinoy
Sr.Counsel

Mr.Daksheesh Dhru
Advocate

Mr. Ahmed Sayed
Advocate
I/b. M/s.Dhru & Co.

Mr. Anand Rathi
Mr. Amit Rathi **for Appellants**

Mr. Goolam Vahanvati
Advocate General of Maharashtra

Ms Rameeza Hakeem
Advocate

Mr. Kumar Desai
Advocate
I/b. Maneksha & Sethna

Mr. Ananta Barua
Jt.Legal Adviser, SEBI **for Respondent**

(Appeals arising out of the order dated 9.11.2001 made by the Securities and Exchange Board of India)

ORDER

These three appeals are directed against the Securities and Exchange Board of India's common order dated November 9, 2001, whereby Shri Anand Rathi (Shri Rathi) (Appellant in Appeal No.52/2001) was restrained from holding any position of director or trustee of any capital market related institutions /entities for a period of two years from March 12, 2001 and the registration granted to Anand Rathi Securities P. Ltd (Appellant in appeal No. 53/2001) and Anand Rathi Direct (India) P. Ltd (Appellant in appeal No. 54/2001), allowing to undertake stock broking business was suspended for a period of nine months. In Shri Rathi's case the order has been made under sections 11 and 11B of the Securities & Exchange Board of India Act, 1992 (the Act) and in the case of the two Appellant companies, it is under regulation 26 of the Securities and Exchange Board of India (Stock Brokers and Sub Brokers) Regulations, 1992 (the Stock Brokers Regulations). While the order against Shri Rathi has the approval of all the three members including the Chairman of the Securities and Exchange Board of India (the SEBI), who heard the matter, the order against the two Appellant companies has the approval of only two members, as one member i.e., the Chairman, did not agree to the conclusion arrived at and the decision taken by the other two members. He has viewed that these two companies are not liable for the penalty of suspension under regulation 26. In terms of section 7(3) of the Act, decision of the majority prevails and therefore the order in force against the two companies is the one made by the two members, being the majority order.

On February 28, 2001, the Hon'ble Finance Minister presented what was widely perceived as an "Investor Friendly" Budget. The general expectation was that the Stock Markets in the country would be encouraged by such a budget, and true to such expectation on February 28 to March 1, the sensex rose by 201 points. However, this rising trend did not continue. On the next day, i.e. on March 2, the sensex dropped by 176 points. There was a lot of consternation and concern as to the cause of such steep fall, which was unusual and exceptional, especially in the light of such a budget. The Respondent initiated investigation into the matter. In that context the Respondent came to know that Shri Anand Rathi, the then President of the Stock Exchange, Mumbai (BSE), had sought some information, at about 1510 hours on March 2, in respect of the position of some brokers / FIIS in certain scrips from the Surveillance Department of BSE. The Respondent decided to investigate the conduct of Shri Rathi also in the said context. As an emergent measure, the Chairman of the Respondent on March 2, by an ex parte Interim Order, restrained Shri Rathi from acting as director-member of BSE and also directed Shri Rathi and his four associate entities (viz. Anand Rathi Securities Pvt. Ltd., Rathi Global Finance Ltd., Rathi Capital & Securities Pvt. Ltd. and Navaratan Capital Securities Ltd.) not to undertake any fresh business as brokers till further orders were passed by SEBI. The order was made under section 11/11B of the Act. Subsequently, a post-decisional hearing was given by the Respondent to Shri Rathi and his associate companies. Three out of the four members who heard the matter, confirmed the order of March 12, Prof.J.R.Verma, the other member though endorsed the majority view in regard to the restraint order on Shri Rathi holding any managerial positions, deferred on the exercise of powers under section 11B to direct Shri Rathi and his concerns not to undertake any fresh business as a broker, interalia, observing that section 11B is a provision, not for punishing intermediaries, but for protecting investors and the market and felt that proceedings must be initiated under regulation 28 of the Stock Broker Regulations for possible imposition of penalties. Subsequently, on the basis of the preliminary investigation report, the order was reviewed and the majority decision was confirmed by the Board on April 23, 2001 and also ordered that an Enquiry Officer be appointed for conducting an enquiry into the matter.

Aggrieved by the majority decision of the Respondent, Shri Rathi filed a writ petition no 628/2001 before the Hon'ble Bombay High Court. The Hon'ble Court, vide its order dated May 2, 2001 dismissed the petition and directed the Respondent to complete the enquiry

within 4 months from the dated of the said order. The time frame provided for passing the order was subsequently enlarged by the Hon'ble High Court, on the Respondent's request. The Respondent passed the impugned order on November 9, 2001.

All the three appeals were filed in the Tribunal on November 20, 2001, pending final decision on the appeals, the Appellants had sought interim order staying the operation of the impugned order. Counsel for the parties were heard in detail in this regard. Taking into consideration all the relevant factors, the Tribunal felt that it was not a fit case warranting interference at the juncture by an interim order and disallowed the prayer vide its detailed order dated November 29, 2001.

Shri Aspi Chinoy, learned Senior Counsel appearing for the Appellants explained briefly the background of the impugned order, and also stated the credentials and achievements of Shri Rathi as well as his contribution to the modernisation of BSE, including the measures taken for strengthening the surveillance system in BSE and bringing transparency in trading transactions. He referred to the first show cause notice issued to the Appellants on June 6, 2001 and stated that even though serious charges were leveled against them, ultimately after the enquiry all those serious charges were dropped and a trivial charge of violating certain circulars was held against the Appellants. Shri Chinoy stated that impugned order is a scrappy order not supported either by facts or law.

Shri Chinoy submitted that the show cause notice dated June 6, 2001 was addressed to Shri Rathi and 4 companies viz. Anand Rathi Securities P. Ltd, Rathi Global Finance Ltd, Anand Rathi Capital & Securities P. Ltd (now known as Anand Rathi Director (India) P.Ltd) and Navratan Capital & Securities P.Ltd. The Enquiry Officer was directed to enquire into the violation by the noticees, of the provisions of

(1) Securities and Exchange of Board of India Act, 1992

(2) (the Act), SEBI (Stock Brokers and Sub Brokers) Regulations, 1992 (Stock Broker Regulations),

(3) SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to the Securities Market) Regulations, 1995 (UTP Regulations)

(4) SEBI (Insider) Trading Regulations, 1992 (Insider Regulations),

(5) SEBI (Portfolio Managers) Regulations, 1992 (Portfolio Managers Regulations),

(6) Various circulars issued by SEBI from time to time particularly with reference to surveillance activities of the exchanges, and

(7) Rules, Regulations and Bye-laws of the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE).

Shri Rathi was asked to show cause as to why action should not be taken against him under section 11B of the Act and under regulation 11 and 12 of UTP Regulations and under regulation 11 of the Insider Trading Regulations. The other four entities were asked to show cause in terms of regulations 25/26 of the Stock Broker Regulations.

The Enquiry Officer submitted his report on September 26, 2001 viewing that Shri Rathi, broker-director and President of BSE sought price sensitive information from the Surveillance Department thereby resulting in erosion of the confidence of investors in the fair, transparent and impartial working of stock exchanges in particular and securities market in general, obtaining such information from the surveillance department Shri Rathi failed to act with the integrity and thus violated code of conduct as broker director and ceased to be fit and proper person under SEBI Regulations; therefore the entities in which he was a director or which were under his control ipso facto ceased to be fit and proper bodies. He recommended that Shri Rathi be restrained from being associated with any of the capital market related institutions/entities for a period of two years. In the case of Navratan Capital & Securities P. Ltd he viewed that it was not a Rathi company and no penalty was recommended. The other 3 companies were found guilty of violation of code of conduct and Regulations pertaining to fit and proper person and recommended that a penalty of suspension of registration under

regulation 28 of Stockbroker Regulations and Regulation 34 of Portfolio Managers Regulations for a period of nine months. Respondent thereafter confirmed the restraint order on Shri Rathi, confirmed suspension of registration of the Appellant companies under regulation 26 of Stockbrokers Regulations and exonerated Rathi Global Finance.

Shri Chinoy submitted that the only charge against Shri Rathi, according to the Respondent, that survived the detailed inquiry, is that he obtained certain price sensitive information from the Surveillance Department on March 2, 2001 which he was not entitled to obtain as per the SEBI circulars and holding that as the ground, by way of penalty a restraint order was passed against him and the registration was suspended in the case of the Appellant companies on the ground that these two companies are "Rathi companies". He submitted that there is not even a suggestion anywhere in the order, that the information obtained by Shri Rathi was used by the Appellants or anybody else for any purpose.

Shri Chinoy stated that on March 2, the Appellant reached his office at the exchange about 2.00 p.m. for a prescheduled meeting that on that day by 3 p.m. senesex was down by 190 points from its previous close, that as the President of BSE, the Appellant was concerned by the said disconcerting drop in the sensex in the background of an investor friendly budget presented in the Parliament on February 28, 2001, and that too the market having responded positively on the previous two days. Learned Senior Counsel submitted that in the light of Shri Rathi's position as the President of BSE it was his duty to monitor and be aware of the causes for abnormal trends in the market, that accordingly he sought to ascertain the broad reasons for such drop in the sensex and also to see whether any remedial steps are to be pressed into service, that at about 3 p.m. Shri Rathi attempted to ascertain the cause for the fall in the sensex from his immediate subordinate and for this purpose he asked his Secretary to connect him on phone to the Executive Director and the General Manager, (Surveillance Department) and that since both were unavailable, the next available person in charge of the Surveillance Department was asked to be connected on phone and the Secretary connected Shri Arun Dhanwade, who was quite new to the working of the Surveillance Department. Shri Chinoy further submitted that upon being connected with Mr. Dhanwade, the Appellant wanted to enquire the broad reasons for such a fall and to ascertain whether there was institutional selling in the 3-4 index stock that had fallen, but Shri Dhanawade being new to the job and also nervous was unable to understand the question and started giving unrelated and unsolicited information, that at no point of time did the Appellant seek any information regarding the prices, volumes or timings of particular transactions or the outstanding position either with regard to any stock or with regard to any broker, that all the information that was given by Shri Dhanawade contained only the names of few selling brokers in a few scrips. Learned Senior Counsel submitted that the bonafide of the Appellant's action is evident from the fact that the telephone call was connected by the Appellant's Secretary at a time when he was in a pre-arranged meeting with six others, including three members of the Governing Board, that this meeting which had commenced sometime around 2.00 p.m. went on till 4.00 p.m. stretching beyond the market closure time of 3.30 p.m., that he had first asked for the Executive Director and General Manager and only in their absence talked to Shri Dahanwade, in an emergent situation. Shri Chinoy further stated that the Appellant himself had requested the Respondent vide letter dated March 7, 2001 to initiate an enquiry to ascertain the facts on the allegations appeared in the news papers of March 7, that the Appellant had sought details of the positions of a leading bull operator and pressed heavy short sales which depressed the market and that on the same day the Appellant on his own stepped down as the President of BSE.

Learned Senior Counsel submitted that as per the statement of charges, forwarded to the Appellant, Shri Rathi has been charged for misusing his official position as President of BSE for personal gains, that Shri Rathi sought to obtain confidential and price sensitive information directly from the Surveillance Department in order to pass the same to trading concerns, either belonging to him / his relatives for their beneficial use. According to him, thus the charge is broadly of misusing the official position, and obtaining price sensitive information for personal benefit. According to the learned Senior Counsel both these charges are unfounded.

Learned Senior Counsel submitted that on March 12, 2001 the Respondent served an order of the same date on the Appellant, stating to be made under section 11 and 11B of the Act restraining him from acting as a director member of the Governing Board of BSE and also prohibiting him and his concerns stated therein from undertaking any fresh broking business, that this order was based on the prima facie view that Shri Rathi had obtained information from the Surveillance Department in breach of certain SEBI circulars, that there was no allegation whatsoever therein that the information sought by him was either price sensitive or that he or

any one else had used the information. Learned Senior Counsel stated that in the order passed on March 30, 2001 after the post decisional hearing confirming the earlier order an effort was made to add an additional allegation namely that the information obtained by the Appellant on March, 2, was price sensitive. Shri Chinoy referred to the subsequent developments including the filing of a Writ Petition by the Appellant and the events followed resulting in the issuance of the impugned order.

Shri Chinoy submitted that the Appellant has been held guilty of breach of three circulars dated August 8, 1995, December 6,1995 and May 25, 2000 issued by the Respondent. He referred to the said three circulars and submitted that as per the circular dated August 8, 1995 it is the responsibility of the management of the stock exchange to detect market manipulations like price rigging etc., and to monitor abnormal price and volume movements, and brokers position, margin, trading limits etc. He submitted that the circular requires immediate and effective action by the Governing Board in an abnormal situation, that the monitoring function assigned to the Governing Board in the circular is not for historical purpose, it means immediate action, that it is in this context and the objectives in view, the exchanges were required to set up separate department- called Surveillance Department. According to him the setting up of the Surveillance Department was clearly to impart administrative efficiency and to assist the management of the stock exchange in its surveillance function. Shri Chinoy further submitted that the circulars clearly envisage regular reporting by Surveillance Department to the Governing Board and that at every Board meeting the functioning of the Surveillance Department is to be reviewed. He stated that the circular dated May 25, 2000 seeks to advise the individual Directors not to interfere or to seek information from the Surveillance Department, that there is no such restriction imposed on the President, which is not accidental but is designed to enable the President to take action in an emergent situation. He pointed out that the stock exchange is required to take remedial measures which can either be taken by the Governing Board or the President alone, and that is why the requirement that if the Surveillance Department observes any abnormality in price movement or in the volume of the scrips traded to immediately report the same to the exchange management. He stated that the subsequent two circulars only re-iterate the position covered in the first circular. Shri Chinoy pointed out that vide circular dated May 25, 2000 the Respondent has clarified that there is no ambiguity as regards the role of the Governing Board with regard to surveillance functioning and has re-iterated that Governing Board would always over see the surveillance functioning in the exchange. Shri Chinoy submitted that the Respondent itself presupposes instances of office bearers coming to possession of confidential and sensitive information as stated in the Respondent's Press release dated January 17, 2001, and hence directed that Directors and functionaries shall refrain from acquiring information other than as may be necessary for discharge of their duties. He stated that the Governing Board is vested with vast powers and as such it does not stand to reason to say that it should not call for information which are required to discharge its duties. In this context he cited the powers of the Governing Board under the bye-laws 71, 72 and 73(a) of the BSE's Bye-laws. He also referred to the special powers of the President under rule 152 of the BSE's Rules, which empowers the President and the Chairman and in the absence of the one, the other to exercise any or all of the powers exercisable by the Governing Board whenever they or he be of the opinion that immediate action is necessary subject to such action being confirmed by the Governing Board within 24 hours. Shri Chinoy also cited the provisions of rule 154 and stated that the special powers of the President under rule 152 does not stand transferred to the Executive Director. In this context Shri Chinoy referred to Shri Rathi's statement of 11th and 12th April 2001, recorded by the investigating officer, elaborately explaining the powers of the President. Shri Chinoy submitted that the Respondent has chosen to ignore the very purpose of the said rules and has interpreted the rules in a manner defying all the reasons, that it is clear from the rules that the Governing Board has to do crisis management and it cannot be expected to do so without the material information before it. According to Shri Chinoy, Shri Rathi had also stated that in the past the Finance Ministry and the Respondent had contacted the President for information relating to market trend and if in the perception of the Government and the Respondent the President was not to have access to the information, then they would not have contacted him. Shri Chinoy submitted that the current theory propounded by the Respondent is not at all tenable in the light of the rule provision read with the ground realities. He said that calling for information from the Surveillance Department which the President is entitled to, is not interference in the functioning of the Department as has been alleged, that on the contrary had the Appellant not acted in the manner as he did on March 2, 2001 he would have been hauled up for being not vigilant. He submitted that the President of BSE was always privy to the matters relating to the Surveillance Department, that all circulars/press releases regarding surveillance have been addressed to the President/Executive directors of the exchange, that

SEBI does not preclude the President of the stock exchange from participating in surveillance related issues, that in fact the President is a member and Chairman of the surveillance committee of BSE, that the Respondent has also acknowledged the fact that the management of the stock exchange, which includes the Governing Board and the President, has complete supervision over the Surveillance Department. In this context he cited the provisions of Bye-law 4,6 and 73(a), rule 118, rule 148, rule 152 and stated that on a careful reading of these provisions it is clear that the President of the exchange is vested with wide and extensive powers for taking vital decisions or actions, for which information is necessary. Mr. Chinoy submitted that though the President is normally a titular head of the Governing Board, under the Rules, Regulations and Byelaws of the exchange an additional responsibility is enjoined upon him whereby he is authorised to take necessary decision with regard to remedial measures, in given circumstances. He submitted that by giving a restrictive interpretation to the circulars and holding that the Appellant fell under the category of individual directors and vested interests and thereby becomes ineligible to obtain information from the Surveillance Department is untenable in the light of the fact that the Appellant was acting in his capacity as President and the action was not meant to obtain any information to his personal benefit, that the fact is that he was required to discharge certain official duties and for the purpose he had to obtain the information. Shri Chinoy, with reference to the Respondent's version that under rule 154 of the BSE rules, the President cannot exercise some of the powers when the Chairman or the Executive Director has been appointed by the exchange, and on the reliance on rule 98 and rule 154 to contend that the President is powerless, stated that the said view is contrary to the settled and established practice which is not only well accepted in the stock exchange but also by the regulating agencies as well as the governmental agencies, that in any event, a proper and harmonious reading of the Rules, Byelaws and Regulations of BSE would show that in case where the Chairman/Executive Director is appointed certain powers of the President of the exchange can be concurrently exercised by the Chairman / Executive Director and the President, that by no stretch of imagination can it be construed that when the Chairman / Executive Director is appointed the President is deprived of his powers and the specified powers solely vest in the Chairman/Executive Director. According to Shri Chinoy, the Executive Director appointed by the exchange, reports to the Governing Board of the exchange with whom the overall management of the affairs of the BSE is vested that the Surveillance Department is only a delegated arm of the exchange. Shri Chinoy submitted that the Respondent holding Shri Rathi guilty of having violated the circular by viewing that he could have contacted the Executive Director, that he did not get his action ratified by the Governing Board, and that he did not take any steps with reference to the market situation even after obtaining the information from the Surveillance Department, is untenable as the President had asked for the Executive Director/General Manager but they were not available and it was even otherwise well within his powers to obtain information in such a crisis ridden atmosphere. Shri Chinoy submitted that since it was felt that no further action was required in this regard, as the Respondent itself had seized of the matter, he did not take any action and since no action was taken by him, there was no need for seeking ratification from the Governing Board.

Learned Senior Counsel submitted that the Respondent has ignored the fact that in the past the Appellant had on many occasions to get in touch with the Executive Director in the context of the erratic movements in the market, as the President is required to be apprised of all unusual price / volume movements, particularly in view of the practice generally being followed on such occasions, the President is required to answer queries from the market regulator and also from the Finance Ministry. The President is therefore required to keep himself apprised with all the developments in the market. In this context he referred to Shri Rathi's reply to a query from the investigating officer that "I have not obtained any information directly from the surveillance department in the past. However, in case of any unusual movements in the market I had received queries from the Finance Ministry and Regulators to find out broad reasons for unusual movements and particularly the behaviour of the FIIs etc". If the President is the contact point to know volatility etc., in the market, then he should have a source to collect the information, that if he has no information, he cannot furnish the information, which he is asked to furnish. He stated that the circulars should be understood taking into consideration the practical realities. Shri Cjinoy stated that the Respondent while proceeding against Shri J.C. Parekh, a former President of BSE, had stated that the President is responsible for the management of the exchange, that now an entirely different stand has been taken in the Appellant's case.

Shri Chinoy stated that 190 points drop in sensex, that too 92 points drop during 2.30 and 3.00 p.m. was alarming and as the President of the exchange, the Appellant was naturally concerned, and it was his duty in the normal course of business to find out the probable

reasons for such an unnatural trend, that it was in that context the Appellant sought information from the Surveillance Department. Shri Chinoy further stated that there was complete transparency and bonafide in the manner in which the Appellant acted as could be seen from the transcript of the conversation, he followed the necessary hierarchy and chain of commands, that first asked for the Executive Director and since he was not available, asked for the General manager (surveillance), that since both of them were not available at that point of time asked his Secretary to connect to a person available, that the call was not made surreptitiously but through the Secretary and in the presence of six other people, that the Appellant very well knew that his telephone conversation with the Surveillance Department would be recorded as he himself was instrumental in installing the automatic voice recording system in the Surveillance Department, that had there been any malafide intention on his part he would not have followed such a transparent course. Shri Chinoy also stated that the call was made from the office of the President at the exchange and not from any private office or from the office of any of his broking entities.

Shri Chinoy stated that in the context of such a sharp fall in the market, in order to understand the probable causes, the first question that would come to the mind of any prudent person is to find out whether it was due to institutional sales or on account of speculative sales, that institutional sales would normally be backed by physical delivery of securities and the risk management measures would be different than if there was excessively speculative selling, that it was in these circumstances that the Appellant enquired whether there was institutional selling. Shri Arun Dhanawade, to whom the Appellant was connected on phone, in the absence of the Executive Director and the General Manager (Surveillance), was not familiar with the function of the Surveillance Department as he was posted to the said department from some other department just 15 days before the event. Shri Chinoy said that it could be seen from the transcript that Shri Dhanwade was not in a position to correctly understand the information which the Appellant was asking, and as such the Appellant tried asking Shri Dhanawade in other ways in order to understand whether there had been institutional selling and being unable to understand as to what the Appellant was asking, Shri Dhanawade on his own started referring to scrips of Himachal, Reliance, Wipro and Global. Shri Chinoy referred extensively to the transcript of the conversation to show that the Appellant had not asked for any broker wise or scrip wise information from Shri Dhanawade. He also stated that the Appellant had asked Shri Dhanawade to ask Shri Reddy (General Manager (Surveillance) to call him up as soon as he came back. Shri Chinoy referred to Shri Tirodkar's statement and said that Shri Tirodkar being the then Director of the Surveillance Department himself in his statement before the Respondent on March 29, 2001 in reply to a question (No.5) had stated that "Shri Rathi has several times asked me about the status of the market particularly when the market were volatile or when there were strong rumours in the market. I have never given any scrip specific or broker specific information to Shri Anand Rathi. To another question (No.7) he had stated that Shri Anand Rathi has not asked any specific information during his term as President". Thus it is clear that in the past also for discharging his duties the President used to call for information from the Surveillance Department and the incident of March 2, 2001 is in no way different. Shri Chinoy reiterated that Shri Rathi obtained the information in the normal course in exercise of his powers as President to discharge his duties, which in no way is in violation of the norms set in the circulars. He said that to hold that the President has no power to elicit requisite information would in effect be to hold that the President has no role in the effective management of the exchanges and such a view cannot sustain in the light of the governing Rules, Byelaws and Regulations of the exchange.

Shri Chinoy further submitted that information obtained by the Appellant was not price sensitive at all, that it was confined only to sales by institutional brokers and at no point of time did he ever ask the purchase position of certain index stocks where the price was crashing fast, that Shri Dhanawade started giving information, which was irrelevant and immaterial and was never asked for. He stated that at no point of time did the Appellant seek any information on the volume, price, timing or outstanding position either of any broker or with regard to any scrip, and no information on long or short positions of any of the brokers was obtained. Shri Chinoy stated that as to what sort of information could be treated as price sensitive has been defined in the Insider Trading Regulations, and that the information sought by the Appellant was not at all price sensitive by any yard stick.

Shri Chinoy denied the charge that the Appellant had sought information from Shri Dhanawade in respect of institutional sales in the scrips of Himachal Futuristic Communications Ltd, Reliance Industries Ltd, Wipro Limited or Global Tele Systems Ltd, as alleged. He stated that it was evident from the transcript that the Appellant did not ask for the information in respect of these four scrips, that Shri Dhanawade himself has in his statement before SEBI officials

stated the reasons for giving this information, though not asked for by the Appellant. He further stated that the reference to Infosys Technologies Ltd and Satyam Computer Services Ltd, has to be read in the context of the overall conversation, the purpose of which was to ascertain, the cause in the fall in the index, that the theme and thrust of the conversation was whether there was institutional selling in 3-4 index scrips that were falling. He stated that supplementary questions were asked only because Shri Dhanawade being new and unfamiliar with the job was not able to give a direct and relevant reply, that infact at no point of time, the Appellant had asked the name of any broker from his side. He pointed out that in fact SEBI itself had asked Shri Dhanawade while recording his statement as to why he had started his reply to the Appellant with the name of CSFB, which the Appellant had not asked.

Learned Senior Counsel submitted that it is wrong to say that the investment activities of institutional investors alone determine the trend of the market as alleged, that the enquiry was made by the Appellant regarding institutional selling as that is backed by deliveries and good for the safety of the market as opposed to the speculative selling. The institutional activity account for only about 10% of the market and is not necessarily indicative of any definite price trend, it is not uncommon that inspite of the buying by the institutions prices keep falling or the prices going up when institutional sale takes place. Similarly all institutions do not take similar views of the market and at the same given point of time if some institutions are selling others may be buying. The learned Senior Counsel stated that infact immediately after the call on March 2, the market actually registered an upward trend and the sensex gained 7.02 points and finally closed at 49616 at 3.30 p.m., that this firmly established that there was no significant movement in the sensex from the time immediately prior to the call, during the call, or after the call. On March 2, 2001 the market closed at 3.30 p.m. The Appellant continued to be in the office upto 4.00 PM even after the closure of the market, that no phone call was made by the Appellant to any of his entities or any other person to convey the information received from the Surveillance Department. Shri Chinoy submitted that thus it is clear that the information was neither price sensitive not it was used for any purpose.

Learned Senior Counsel stated that the Respondent has ignored the fact that the enquiry report absolves the entities of having used the information for the purpose of trading or otherwise and has wrongly persisted with a presumption that the purpose of gathering information was to pass it to entities and was to use it for trading purposes. Shri Chinoy submitted that this is nothing but a conjuncture and far away from the truth. He referred to the Respondent's observation that "As the fall continues, there was perhaps no necessity fore taking any further position by his associate entities" and stated that it is only a baseless presumptive inference. He stated that infact the market had gone up between 3.00 p.m. and 3.30 p.m. and therefore the observation "as the fall continues" is contrary to the facts on record. He further stated that the Respondent's observation that there was no necessity for taking any further position also presumes that a certain position was already taken, for which there is no evidentiary supporting and in case there is anything to indicate the position, if any taken, there is nothing to show that the same was based on such information.

Learned Senior Counsel submitted that the Respondent is not justified in holding that the Appellant had sought information in relation to or for the benefit of his associate concerns or for trading, when it had come to the conclusion that there was no use of information. He said that the eight -month long detailed investigations had revealed that the information had not been used or utilised either by Shri Rathi or by any of his entities.

Shri Chinoy submitted that the very enquiry based on the findings therein, the impugned order was passed is illegal in as much as during the course of enquiry the Enquiry officer had refused the Appellant's request for cross examining some of the persons whose statements have been recorded during the enquiry and on which relevance has been placed during the enquiry and in the report, that the denial of a right to cross examine was in flagrant breach of the principles of natural justice. Further, the learned Senior Counsel submitted that the Respondent had deliberately not furnished a copy of the preliminary report and even as regards the final investigation report, the Appellant had been furnished only the findings, that it is thus clear that even during the course of the enquiry and thereafter the Respondent acted in breach of the principles of natural justice and fair play, that the very fact that the enquiry / investigation report is sought to be suppressed and / or kept back goes to show that there is much more than meeting the eye that if the same is disclosed it will not support the conclusions and decisions arrived at by the Respondent.

Shri Chinoy pointed out that even though the show cause notice dated September 27, 2001 refers to a penalty of a ban of two years, the Respondent has changed its stand in the order by

stating that such a ban is not a penalty at all and that the Respondent is authorised to issue such an order not only as a preventive measure pending enquiry, but also by way of a final order. Shri Chinoy submitted that the impugned order is clearly in the teeth of the recent decision of this Tribunal in Sterlite Industries Ltd v. SEBI (2001) 34 SCL 485: (2001) 45 CLA 195) wherein it has been expressly held that under section 11 and 11B the Respondent has no powers to impose penalty, that a patently untenable stand has been taken by the Respondent by saying that the impugned order does not amount to penalty. Shri Chinoy submitted that the Respondent's change in version is to get over the obvious difficulty of a binding authority of this Tribunal, that even otherwise the view of the Respondent that the imposition of the ban of this nature does not amount to penalty completely overlooks the fact that as compared to pecuniary penalty which is of a specific amount, such kind of a ban has the effect of completely denying or taking away the Appellant's right to trade and carry on the business and this is of far reaching adverse consequences as compared to pecuniary penalty.

Shri Chinoy submitted that the Respondent has penalised Shri Rathi in the guise of a direction under section 11B of the Act. In this context he referred to the word "penalty" used in the show cause notice. Shri Chinoy extensively quoted from the Tribunal's order in Sterlite case on the test of evidence required for imposing penalties and also on the scope of section 11B. He submitted that the instant order is neither preventive nor remedial but punitive. He submitted that by preventing the Appellant holding any position as a director or trustee in a market entity, the order is not rectifying or remedying anything. Shri Rathi's conduct as a broker or having bearing on broking activity has not been questioned in the order, that the charge against him is that he had violated the requirements of certain circulars. Shri Chinoy stated that the various offences referred to in section 15A to 15H does not cover violation of any circulars as an offence. He also referred to the provisions of section 15J required to be followed while imposing penalties. Re-iterating his view that the Respondent has imposed penalty on the Appellants, he referred to the principles laid down by the Hon'ble Supreme Court in Hindustan Steels v. State of Orissa (AIR 1970 SC 253) and stated that none of the factors warranting imposition of penalty stated in the said case is available in the Appellant's case as it is evident from the evidence that the Appellant had acted openly and bonafidely and did not violate any of the legal provisions. He cited Khemka and Co. (Agencies) v.State of Maharashtra (AIR 1975 SC 1549) to show that an offence cannot be created by a circular, that on the contrary the law casts a duty on the President of the exchange to discharge certain duties and he has only discharged those duties and proper discharge of duties should not be considered as an offence or failure. He stated that on the contrary if the Appellant had failed to discharge the statutory duties cast on him, he would have faced the charge of dereliction of duty and the attendant consequences. Shri Chinoy cited decisions of the Hon'ble Supreme Court in support of his contention that it is necessary to establish mens rea for imposition of penalty – Akbar Badruddin Jiwani v. Collector of Customs (1990 (47) ELT 161 SC) and also the decision of the Hon'ble Calcutta High Court in Extrusion v. Collector of Customs (1994 (70) ELT 52 (cal).

With reference to the reliance by the Respondent on this Tribunal in R.K. Aggarwal v. SEBI (2001) 31 SCL 271: (2001) 42 CLA 254, the learned Senior Counsel stated that the facts in that case were clearly different from the facts in the present case. He explained the distinguishable features of the cases and stated that the view taken by the Tribunal in the said case cannot have any application to the present case.

With reference to the appeals filed by the two companies, Shri Chinoy submitted that the Appellants have been penalised on the sole ground that Shri Rathi, who is stated to be controlling the Appellants, had violated the SEBI circulars by allegedly interfering with the working of the Surveillance Department, that the Appellants have not complied with the requirements of fit and proper person criterion under the Stock Brokers Regulations. Learned Senior Counsel submitted that the charge against Shri Rathi itself is untenable and that in any case such a vicarious imposition of penalty on the Appellants despite the fact that the Appellants are not involved in any way in the acts / breaches alleged is illegal and unjust. He submitted that the Respondent has ignored the fact that Shri Rathi as the President of BSE had made the telephone call, that Rathi has not made inquiries with the Surveillance Department on behalf of the Appellants, that there is no evidence to show that Shri Rathi was acting in the course of his employment / position with the Appellants or that such actions were actuated with a motive to benefit the Appellants. He stated that the Appellants are separate legal entities and could not be held vicariously responsible for the activities of Shri Rathi, more so when the actions are not even in the course of discharge of his duties on behalf of the Appellants. Shri Chinoy referred to the Respondent's version that the broking entities controlled by Shri Rathi in which he is a director would also not be considered as "fit and

proper" as the artificial entities such as corporate entities actually act through their directors and employees only, and therefore, the conduct of their directors has a bearing as to whether the corporate entity is fit and proper or not, and stated that this contention is baseless. Shri Chinoy submitted that the concept of lifting the corporate veil was introduced inorder to identify and implicate the offending director hiding behind the corporate veil for the wrongs committed in the name of the corporate entity but never to make the company liable for the acts of a director acting in any other capacity unrelated to the company's functions. He submitted that the Respondent has not raised any specific allegation of violation of the integrity requirement of the code of conduct or that the Appellants have failed to maintain high standards of integrity, promptitude and fairness in the conduct of its business and admittedly there is no specific complaint or evidence in this behalf.

Shri Chinoy submitted that the Respondent inflicted penalty on the Appellant for the alleged breach of circulars and there is no charge of misuse of information. He referred to the observation in the enquiry report that "the conduct of Shri Rathi in seeking information and denial of allegation etc. shows that he had sought information in relation to his broking activity. Seeking of such information per se is in violation of SEBI circulars. Procuring of such information amounts to interference in the working of surveillance department which reflects adversely on the fairness, transparency and impartial working of stock exchanges and also undermines confidence of investors in securities market". He referred to the further observation in the enquiry report that Shri Rathi "has not explained the purpose for which he took the information. The nature of information procured by him and his subsequent conduct such as not disclosing the fact of conversation on his own and denial of reports in the news papers in respect of conversation shows that the information was actually taken for the benefit of his broking entities". Shri Chinoy submitted that the said view is contrary to the facts before the Respondent as Shri Rathi had clearly explained the back ground and purpose of seeking information and that he did not deny that he had not spoken to the Surveillance Department, that the rejoinder to the report in the newspaper was with reference to his alleged conversation with Shri Garella.He stated that in the same enquiry report it has been stated that the preliminary investigation establishes that Shri Rathi had obtained price sensitive information from the exchange, he was an insider and that the entities associated with Shri Rathi have traded in some scrips on March 2, 2001 and on March 5, 2001, details of which has been given in the show cause notice dated June 6, 2001. However it is not clear whether the said trading in those scrips was done on the basis of information obtained by Shri Rathi from Shri Dhanawade. Therefore it cannot be said with certainty that the said trading by Shri Rathi and noticees had been done on the basis of said information. I am therefore giving them a benefit of doubt in regard to violation of regulation 4 of the SEBI (Insider Trading) Regulations, 1992. It may however be mentioned that SEBI is appointing an independent agency to examine whether the trading by the noticees was based on the said information". Shri Chinoy further referred to the report wherein the Enquiry Officer had stated that "In view of the finding in above paras I am of the considered view that Shri Rathi obtained price sensitive information which was unpublished. This information if used for trading in a substantial manner would result in artificially raising or depressing the prices of securities thereby inducing common investors to sell or purchase the securities. The same would have been in violation of the Regulation 4 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to the Securities Market) Regulations 1995. The preliminary investigation shows that the associate entities of Shri Rathi traded in some scrips. However, there is inadequate material to show that this particular unpublished price sensitive information was used for the said trading. Further the preliminary investigation also does not throw much light on the direct effect of the said trading in depressing or increasing the price in a significant manner. I therefore give benefit of doubt to Shri Rathi and the noticees in respect of charges for violation of Regulation 4 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices in the Securities Market) Regulations, 1995. It may however be mentioned that SEBI is appointing an independent agency to examine the use of the information and its effect on the price". In this context Shri Chinoy stated that the observation made in the order is contrary to the factual position revealed in the enquiry report. He stated that in para 12.9 of the order it has been stated that "the Enquiry Officer concluded that the information sought by Shri Rathi was in relation to or for the benefit of his associate concerns or for trading. As the fall continued there was perhaps, no necessity for taking any further position by his associate concerns". Shri Chinoy submitted that it is, thus evident that this is a conjuncture and a person cannot be penalised on the basis of conjunctures and surmises.

Shri Goolam Vahanvati, learned Advocate General appearing for the Respondent submitted that it is not in dispute that Shri Anand Rathi, the then President of BSE contacted the Surveillance Department of BSE on March 2, and obtained trade related details in breach of

the governing directions, and Shri Rathi was not unaware of the circulars issued by the Respondent in this regard restraining persons, other than the specially designated officers, from accessing the surveillance set up in the exchanges.

Learned Advocate General stated that the very purpose for which the Surveillance Department was set up and the reasons for its being immunised from the invasion of trading interests who run the exchanges like BSE, can be found in the circular issued by the Respondent requiring the exchanges to set up separate and independent Surveillance Department. He submitted that it is the duty of the exchanges to protect the interests of all concerned dealing in securities and not the interests of the broking community alone, that the stock exchange is not a private club of the brokers. He explained the role of the Surveillance Department and the reason as to why the information available therein are not made available to any traders, that if a particular trader, be a director / President of the exchange, allowed access to the Surveillance Department he would be in a better position with information over others in the market and that information could be used to his betterment, thus for providing a "level playing ground" to all the persons, the access to Surveillance Department is restricted only to the few designated officers having no personal trading interests. Learned Advocate General stated that any attempt to procure information from the Surveillance Department is unacceptable irrespective of the fact whether such an action could be termed interference or not. In this context he referred to the circular dated August 8, 1995 issued by the Respondent to the exchange authorities on setting up of market Surveillance Department in stock exchanges and stated that in the said letter it has been stated that "one of the important issues discussed during the meeting of the Executive Directors of Stock Exchanges with SEBI on 19th July, 1995was regarding requirement of market surveillance of stock exchanges". Learned Advocate General stated that from day one, it was the Executive Director, not the President, who was put in position in the matters relating to setting up of the Surveillance Department. In support of his contention that the President was out of picture, he read out the portions from the said circular that "During the discussions it was emphasised by the Chairman that it is the responsibility of the stock exchanges to detect market manipulations like price rigging etc., and to monitor abnormal price and volume movements which are non-consistent with normal trading pattern. It is also the responsibility of stock exchanges to monitor brokers position, margins, trading limits etc., to ensure that the brokers do not commit default adversely affecting the market and the interest of the investors."Learned Advocate General stated that the object of setting up the Surveillance Department is thus clear that it is to ensure that the brokers do not commit default to the detriment of the market and the investors. He further referred to para 1.3 of the circular and stated that to achieve the said objective and to ensure proper and orderly functioning of the markets, the circular directed that "Each of the Stock Exchanges shall have separate surveillance department entirely devoted to carry out the functions indicated in the circular". These functions are (1) monitor price movement of scrips including price rigging, other market manipulations etc. and immediately highlight any abnormality therein to enable the stock exchange management to take effective measures like applying of circuit breaker, suspension of trading and / or investigation if necessary, (2) monitor volumes of scrips traded and immediately highlight any abnormality therein to enable the stock exchange management to take effective action of the types mentioned in (1) above, (3) monitor any abnormal changes in brokers position compared to normal trading pattern of the broker, (4) monitor evasion of margin payment by brokers, (5) monitor violations of trading restrictions and limits by brokers, (6) monitor any other abnormality which is detrimental to the integrity of the markets and the interest of the investors". The circular also specifically directed that "Surveillance Department shall not be saddled with any other responsibility and that the department will be directly under the Executive Director of the stock exchange or senior most officer of the stock exchange in his absence". Learned Advocate General stated that it is thus very clear that the Surveillance Department is as forbidden territory for brokers and vested interests to enter, that a broker director / office bearer of the exchange is not an exception. He submitted that on a perusal of the circular it is very clear that the obligation is cast on the Surveillance Department and not on any particular office bearer like director / President to monitor the development, that the circular itself empowered the Surveillance Department to take corrective measures in a crisis independent of intervention by anybody else. He also submitted that the reference to stock exchange management in the circular should be understood in the context of the purpose for which the Surveillance Department is set up and the powers vested in the Executive Director in terms of the rules and the bye-laws of the exchange.

Learned Advocate General referred to the circular dated December 6, 1995 issued by the Respondent and stated that the said circular also reiterated that the Surveillance Department

should be independent, as has been stated therein that "there is no need to repeat that we attach utmost importance to the activity of the market monitoring and market surveillance for ensuring integrity and transparency of the market which is essential for building up investor confidence…. It is re-iterated that the Executive Director would be directly responsible for the proper and independent functioning of the surveillance department."

Learned Advocate General also referred to the subsequent circular of May 25, 2000 and stated that the said circular also reiterated that the Surveillance Department is independent and separate. He read out the following portion from the circular in this regard " The issue of the role of the Governing Board with regard to surveillance functioning of the exchange was discussed and it was clarified that there is no ambiguity as far as the overall role of the Governing Boards. In this context reference was drawn to earlier SEBI circular No.SMD/3953/96 dated August 17, 1995 and wherein SEBI had directed the Governing Boards of the exchanges to review the functioning of their surveillance department at every Board meetings. As regards the responsibility of the Executive Director, since surveillance is a very important and sensitive area, it was stipulated that this would be under the direct responsibility of the Executive Director who is the senior most executive of the exchange. It was also advised earlier that there should be no interference in the functioning of the Surveillance Department, which should be done in a very professional and objective manner. The spirit behind such stipulation was that there should be no interference from individual directors, member brokers or any other vested interest and there was never any doubt that the Board as a whole would oversee and give policy directive to the surveillance functioning in the exchange". He stated that the circular thus clearly bans member brokers and vested interests interfering in the functioning of the Surveillance Department. Learned Advocate General submitted that it is clear that nobody is entitled or empowered to call for information from the Surveillance Department and the word interference should not be interpreted in the technical sense but in a realistic sense in the context in which it is used. The purpose of setting up of the Surveillance Department would be defeated if the confidentiality of the data is not preserved by making the same available to the trading interests.

With reference to reliance placed by Shri Chinoy on the emergency powers available to the Governing Board, under the Rules of BSE, the Learned Advocate General pointed out that in terms of rule 154(a) the emergency powers are vested in the Executive Director and not in the Governing Board or the President. He stated that in terms of the said rule 154 whenever a Chairman / Executive Director is appointed the powers, rights, duties and functions of the President as provided in the Rules, Bye-laws and Regulations of the exchange, save and except those under certain specific rules stated in the rule itself, vest in and shall be deemed to be the powers rights duties and functions of the Chairman, that no power under any bye-laws or regulations has been excluded by the said rule 154. Referring to Shri Chinoy's submission that rule 152 is a special power vested in the President to meet emergent situations, the learned Advocate General stated that under the said rule President and the Chairman and in the absence of the one, the other shall be entitled to exercise any or all of the powers exercisable by the Governing Board whenever they or he be of the opinion that immediate action is necessary. He said that the rule is on the powers exercisable by the Governing Board, and that in the present case it is not a matter in which the Governing Board has any power to interfere and therefore the President in the absence of Chairman exercising the power which is not vested in the Governing Board did not arise, that even otherwise since the Executive Director was well available the President was ineligible to take solo action in the matter and the power, if any, at all could be exercised only jointly with the Executive Director and not by the President alone. In this context he referred to the provisions of rule 98. As per the said rule:

> **"whenever a Chairman is appointed as hereinafter provided he shall be an ex-officio Member of the Governing Board in addition to the (nine elected) Members of the Governing Board. The Chairman shall not while he continues to hold that office be subject to retirement but he shall cease to be a Member of the Governing Board if he ceases to hold the office of Chairman. Provided that when the Securities and Exchange Board of India so desires the Governing Board shall appoint a whole time Executive Director and the appointment of such Executive Director, the terms of his appointment and his removal or dismissal from office shall be subject to the previous approval of the SEBI. The person appointed as Executive Director shall not engage himself in any business directly or indirectly during his tenure of office and if he is a member of the exchange at the time of appointment he shall resign his membership forthwith. The Executive Director shall be an ex-officio Member of the Governing Board and of any committee appointed by the Governing Board of the Exchange. Subject to the over-all**

management of the affairs of the Exchange being vested in the Governing Board as provided in these Rules, Bye-Laws and Regulations the Executive Director shall be vested with the executive powers of the Exchange to run the day-to-day administration and to enforce the Rules, Bye-laws and Regulations of the Exchange and to represent the Exchange in any public matter and to exercise all other powers, rights, duties and functions as are vested in the Chairman under the Rules, Bye-laws and Regulation of the Exchange and as may be entrusted or delegated to him by the Governing Board from time to time. It shall be the duty of the Executive Director to give effect to the directives, guidelines and orders issued by the Securities and Exchange Board of India in order to implement the applicable provisions of law, rules and regulations as also the Rules, Bye-laws and Regulations of the Exchange."

He also referred to rule 149 under which " the executive powers of the exchange shall be vested in the Chairman who shall direct the enforcement of the Rules, Bye laws and Regulations of the exchange and have the care of all its interest", and stated that assigning the Surveillance Department's control to the Executive Director by the Respondent vide its circulars is perfectly justified.

Further, the learned Advocate General stated that if Shri Chinoy's submission is accepted, it would mean that every time the market index falls, the President can access the Surveillance Department and if that is acceptable the very need for having a separate and totally independent outfit exclusively under the Executive Director may not be of any necessity. Learned Advocate General pointed out that the surveillance system was strengthened and for the purpose a separate out fit – Surveillance Department – in each exchange was set up and it was kept out of reach of the member brokers etc to monitor the activities of the brokers to protect the market and the interests of the investors, when the situation demands. Surveillance Department is not meant to serve as an information center to the President or the directors, having broking interests in the market. He submitted that since the Rules and Bye laws naturally, were in position much before 1995 it is futile to look for any specific provisions governing the Surveillance Department therein, that the powers of the Governing Board under the Rules, Regulations and Bye laws should be read in the context, with reference to the circulars stated above. He submitted that there is no denial of the fact that the Surveillance Department is a part of the exchange and the Governing Board has the power to review its function, that this fact has been accepted by the circular also, but the power for reviewing the functioning of the department cannot be construed as the power to accessing information monitored in the Surveillance Department.

Learned Advocate General submitted that the circulars referred to in the impugned order are issued by the Respondent well within its powers under section 11 and they are binding on the parties and in the event of their breach consequences would visit the person breaching the same.

Learned Advocate General stated that even as per the admission of the Appellant himself, he reached the exchange at 2.00 p.m. to attend a pre-scheduled meeting that he was aware of the index fall contrary to all expectations, that by 3.p.m. the sensex had dropped by 190 points from the previous close. Referring to the conduct of Shri Rathi learned Advocate General stated that Shri Rathi contacted the Surveillance Department at 3.10 p.m. knowing very well that normally market closes at 3.30 p.m., and he also knew that it was the last day of the settlement and the next two days being Saturday and Sunday the markets would remain closed and still he claims that he was only collecting information for crisis management and according to him the matter was of so much urgency and he could not wait for the Executive Director or General Manager who were in the Respondent's office, a few blocks away from the exchange, to come and that there was no time even to contact them on their mobile phones. Learned Advocate General submitted that the Appellant is only trying to put up a story for general consumption, which is nothing but a story - an alibi to defend his action - that he contacted the Surveillance Department as the matter was very urgent, though there was no urgency as such at that point of time.

Learned Advocate General read out the entire transcript of the telephonic conversation the Appellant had with Shri Dhanawade and stated that the conversation by itself does not indicate any sense of urgency, as is evident that Shri Rathi was stretching the conversation to find out information from Shri Dhanawade. He pointed out that if the Appellant was concerned only about the institutional sales as he claims, he should have stopped further inquiries the moment his starting query on the institutional sales was answered by Shri Dhanawade by saying that "basically the operators are selling", but instead of closing the conversation he

went on probing further about scripwise such as Satyam, Infosys and also broker wise. He stated that on a perusal of the transcript it is difficult to believe that the Appellant was seeking information for any crisis management purpose. He pointed out that the Appellant could not wait for the General Manager to come from the Respondent's office, he did not have time to talk to him on the mobile phone, but he was merrily dragging on the conversation with a junior officer of the Surveillance Department, who was too willing to pour out the information, that his conduct is thus self revealing of the purpose for which he contacted the Surveillance Department. Learned Advocate General stated that the Appellant's letter of March 7, 2001 to the Respondent is only an eye wash and merits no consideration as he did not deny therein the fact of obtaining information from the Surveillance Department but only stated that Mr. Garela is not the chief of Surveillance Department and he did not talk to him, that the request to SEBI to institute proper enquiry into the matter was meant only to deflect the heat of the moment on him.

Learned Advocate General re-iterated that the Appellant had chosen the right time to obtain information from the Surveillance Department to benefit him and his broker entities, as he sought the particulars at 3.10 p.m. on the last day of the settlement and the following two days were holidays. The question whether he made use of the information or the information so obtained was found useful to him are not issues which could absolve the Appellant of the charge of doing something forbidden. Learned Advocate General stated that Shri Rathi contacted the Surveillance Department in the presence of other brokers with scant regard to the confidentiality involved and by obtaining the information to get an unfair advantage over others and through him to the broker entities owned and controlled by him. He submitted that it was gross impropriety on the part of the Appellant to call for the details as he did on March 2, 2001.

Learned Advocate General submitted that this Tribunal has already upheld the action taken by the Respondent in R.K.Aggarwal's case, in the context of Shri Aggarwal's action vis-à-vis the Surveillance Department of the UP Stock Exchange. He submitted that the present case is fully covered by the said decision. Learned Advocate General further submitted that Shri Rathi is a nominee of the corporate entity belonging to him and he did not become a member of the Governing Board and the President of BSE in his personal capacity. In this context he referred to rule 100A of BSE Rules and stated that the corporate entity, which nominated the Appellant, cannot fully absolve itself for the actions of its nominee.

Learned Advocate General stated that an impression is being made that the Appellants have been penalised by invoking the provisions of section 11B of the Act, against the view taken by this Tribunal on the scope of Section 11B in the Sterlite case. He stated that in the case of Shri Rathi the direction is that he be restrained from holding any position of Director or trustee of any capital market related institution/entities for a limited period of 2years. Such a restraint order by any standard cannot be treated as a penalty. In the case of the two Appellant companies, their registration as stock brokers was suspended in terms of section 12(3) of the Act read with regulation 29(3) of the Regulations following the prescribed procedure, that in terms of the provisions of regulation 26 the Respondent is empowered to impose a penalty of suspension of stock broker. Learned Advocate General pointed out that the "reference to penalty as recommended by the Enquiry Officer" in the show cause notice dated September 27, 2001 should be read in the context of the recommendations of the Enquiry officer, that the Enquiry Officer did not recommend any penalty against Shri Rathi but only recommended that "Shri Rathi be restrained under section 11 and 11B of the SEBI Act, 1992 from being associated with any of the capital market related institutions / entities", and he recommended "a penalty of suspension of registration" in respect of the other two Appellants, that it is also to be noted that the notice was not addressed to Shri Rathi alone, but it was a combined one addressed to 5 other broking entities. The learned Advocate General submitted that the restraint orders made against Shri Rathi is a measure in terms of section 11 / 11B and not a penalty, that he is not debarred from doing business, that the debarment is only on Shri Rathi participating in the management of capital market related institutions as a director or trustee. He also stated that various High Courts have upheld the Respondent's power under section 11 and 11B to take appropriate measures for the purpose of the Act, and he particularly referred to Anand Rathi v. SEBI (2001) 43 CLA 312 decided by the Hon'ble Bombay High Court. Learned Advocate General also pointed out that in the case of J.C.Parekh, a former President of BSE the direction issued in the light of the conclusion arrived at by the Respondent that Shri Parekh had been acting in a manner unbecoming of the post of President of BSE, and in that context Shri Parekh was held ineligible to hold any public position as member of the Governing Board or the office bearer of the exchange as well as capital market related public institutions for a period of three years and the said direction was upheld by the

then existing Appellate Authority in the Finance Ministry. The appeal filed by Shri Parekh against the said order in the Hon'ble Bombay High Court is pending and the Court did not grant any stay of the operation of the said order, despite Shri Parekh's prayer.

Referring to Shri Chinoy's submission on the need for proving mens rea, the learned Advocate General stated that in a matter like this element of mens rea is not required to be established as has been held by the Hon'ble Supreme Court in Director of Enforcement v. MCTM Corporation P.Ltd (AIR 1996 SC 1100) and therefore the authorities cited by the Appellants in this regard is of no relevance to the issues under consideration in the appeal.

With reference to the suspension order made against the two Appellant companies the learned Advocate General submitted that since Shri Rathi being a nominee of the corporate entity and the two Appellant companies are owned and controlled by him, and in the light of the finding that Shri Rathi is not a fit and proper person, the suspension of the entities owned and controlled by him is justified. He submitted that the action / conduct of Shri Rathi is to be taken into consideration in this context, and as disclosed in the order that his conduct and his action has caused erosion of investor confidence in the fair, transparent and impartial working of stock exchanges. Learned Advocate General submitted that the conduct of Shri Rathi in obtaining sensitive information from the Surveillance Department in breach of the circulars is a serious matter and the action taken by the authorities cannot be faulted on any account.

Learned Advocate General refuted the allegation that the impugned order was made without following the principles of natural justice. He stated that the Appellants have been given more than sufficient opportunities to defend their case by issuing detailed show cause notice, and by furnishing enquiry report and materials on which reliance was placed by the Respondent, and in no way they were debilitated in putting forth their version. The Appellants were not only allowed to make written submissions but were heard extensively and their submissions were duly considered.

I have carefully considered the submissions made by the parties. My views are discussed herein below:

Even though Shri Chinoy had stated that the Respondent had failed to follow the principles of natural justice, he did not press the same.

The controversy in the present case centers around the telephone call made by Shri Rathi, the then President of BSE, to Shri Dhanawade in the Surveillance Department of BSE on March 2, 2001. The said March 2, is not just an ordinary date, it was a day of mayhem as far as BSE was concerned. The capital market, true to the expectation was responding positively to the Union Budget 2001, presented to the Parliament on February 28. Though the market was buoyant on February 28 and March 1, and the sensex rose by 201 points, to everybody's dismay it took a reverse turn on March 2. Sensex dropped by 176 points. Bear hammering by few was one of the causes attributed to the market casuality. Innocent investors suffered heavily. Credibility of the market lost. The Respondent mandated to protect the interests of the investors and responsible for regulating the securities market, smelt a rat and decided to investigate into the matter. In that surcharged atmosphere some news papers carried out stories alleging that Shri Rathi had illegally obtained some price sensitive information from an officer of the Surveillance Department in the presence of some brokers. Since Shri Rathi himself had trading outfits in the market, the Respondent felt that the allegation merited investigation. Investigation started. The Respondent obtained the taped conversation Shri Rathi had with the official of the Surveillance Department. The transcript of the telephonic conversation established that Shri Rathi had talked to one of the junior officials in the Surveillance Department and it also revealed that he had obtained from him information in respect of certain specific scrips and brokers. The Respondent after detailed investigation and enquiry came to the conclusion that Shri Rathi had collected price sensitive information from the Surveillance Department of BSE in breach of the governing norms and considered him as "not a fit and proper person" to be associated with the management of the exchange etc. In that context not only Shri Rathi was restrained from participating in the management of the capital market related institutions and entities as a director or trustee but two of his companies were penalised by suspending their registration for nine months. The said nine-month period is already over and the suspension order is no more in operation. Thus the sting is no longer there, but the stink still continues as the finding of guilt continues. That is why the Appellant companies are seeking relief.

Shri Rathi has questioned the basis and validity of the findings and the order on several

grounds, particularly on the ground that he had lawfully obtained the information in his capacity as the President of the exchange and that as per the governing rules and bye-laws of the exchange, the President is entitled to access the Surveillance Department to obtain information that he had not used the information for any personal benefit.

A stock exchange is not a mandi of the sort free for all. It is a sensitive forum providing a level playing ground to all the participants, facilitating transactions involving multitude of investors and crores and crores of rupees having a bearing on the economy as a whole. The regulatory regime is designed and structured in such a way to ensure that nobody takes undue advantage by virtue of his position in the management of the exchange. Good governance of stock exchange being essentially necessary to protect the interest of all the market players including the investors, the exchange is subjected to several statutory regulations. The Securities and Contracts (Regulation) Act, 1957 (SCRA Act) and the Rules made thereunder provide the broad statutory frame work. The Rules, Bye laws and the Regulations made by each stock exchange provide for regulating the activities of the exchange. In the hierarchy it is the Governing Board which is vested with most of the powers. The Board consists of elected and nominated members. One of the elected members is elected as the President of the exchange for a tenure not exceeding one year at a time. The Chief Executive of the exchange is Chairman / Executive Director who is supposed to be independent of any personal trading interest in the securities dealt on the exchange. The exchange admits corporate and non-corporate members. The two Appellant companies are corporate members of BSE.

Shri Rathi was elected to the Governing Board of BSE as a nominee of Anand Rathi Securuities P.Ltd, a corporate entity owned and controlled by him. He was elected as the President for the period 1999-2000 and again for the year 2000-2001. During the crisis period referred to above Shri Rathi was the President. The two other Appellant companies are private limited companies owned and controlled by Shri Rathi / his family. Anand Rathi Securities P. Ltd, (Appellant in appeal No.53/2001) is a stock broker, merchant banker and port folio manager and holds certificate of registration from the Respondent to do the said business. Anand Rathi Direct (India) P. Ltd is a sub broker and holds a certificate for the purpose.

The Respondent is a statutory body established under section 3 of the Act. It is mandated to protect the interests of investors in securities and to promote the development of and to regulate the securities market and for matters connected therewith or incidental thereto. Section 11 of the Act enumerates the functions of the Board. Section 11B enables the Respondent to issue directions to certain persons for certain purposes. The Respondent has made several regulations to regulate the activities of the market intermediaries including stockbrokers, merchant bankers, portfolio managers etc. Regulatory powers of stock exchanges under the SCR Act are also vested in the Respondent.

The Respondent in its effort to protect the interests of the investors and to ensure fair dealings in the market by providing a level playing ground to market participants decided to have a strong and independent Surveillance Department in each stock exchange and devised a set up immune to interference from brokers. This requirement was discussed by the Respondent in the meeting of the Executive Directors of stock exchanges held on July 19, 1995, and based on the decisions arrived at therein issued a circular to all the stock exchanges, requiring them to set up an independent Surveillance Department out of the reach of the market players. Since both the parties had placed considerable reliance on this circular and two other circulars, which followed, it is felt that it would be advantageous to extract the text of these circulars for ready reference. The first circular issued on August 8, 1995, which is the basic charter, reads as under:

> **" SUB: SETTING UP OF MARKET SURVEILLANCE DEPARTMENTS IN STOCK EXCHANGES**
>
> **One of the important issues discussed during the meeting of the Executive Directors of Stock Exchanges with SEBI on 19th July 1995 was regarding requirement of market Surveillance by Stock Exchanges.**
>
> **1.1 During the discussions, it was emphasised by the Chairman that it is the responsibility of the Stock exchanges to detect market manipulations like price rigging, etc. and to monitor abnormal price and volume movements which are non consistent**

with normal trading pattern. It is also the responsibility of Stock Exchanges to monitor broker's positions, margins, trading limits, etc. to ensure that the brokers do not commit defaults adversely affecting the market and the interest of the investors.

1.2 It is noticed that at present, barring one or two, Stock Exchanges do not have a separate market surveillance department and therefore the above mentioned functions of market surveillance are not carried out in a systematic, objective and effective manner.

1.3 In the context of the above and to ensure proper and orderly functioning of the markets, it is directed that:-

(a) Each of the Stock Exchange shall have separate surveillance departments entirely devoted to carry out the functions indicated in the para (b) below.

(b) The surveillance department shall :

(i) Monitor price movement of scrips including price rigging, other market manipulations etc. and immediately highlight any abnormality therein to enable the Stock Exchange management to take effective measures like applying of circuit breaker, suspension of trading and/or investigation, if necessary.

(ii) Monitor volumes of scrips traded and immediately highlight any abnormality therein to enable the stock exchange management to take effective action of the types mentioned in (i) above.

(iii) Monitor any abnormal change in broker's position compared to normal trading pattern of the broker.

(iv) Monitor evasion of margin payment by brokers.

(v) Monitor violations of trading restrictions and limits by brokers.

(vi) Monitor any other abnormality/eventuality, which is detrimental to the integrity of the markets and the interest of the investors.

(c) This department shall not be saddled with any other responsibility so that it can concentrate on the functions mentioned in para (b) above.

(d) This department will be directly under the Executive Director of the stock exchange or senior most official of the stock exchange in his absence.

1.4 On the issue of connectivity and reporting to SEBI separate format will be worked out and sent to Stock Exchanges. The Executive Director and in his absence the senior most official of the Exchange will ensure timely reporting to SEBI.

1.5 The proposed surveillance department shall set up by Stock Exchanges latest by 30th September 1995. A compliance report to giving details of the setting up of the surveillance department will be sent to SEBI immediately thereafter by the Executive Directors/ Presidents of the respective Stock Exchanges."

The Respondent issued another circular to the exchanges (2nd circular) on December 6,1995, which reads as under:

"As you are aware vide our letter No. IEMI/LKS/MI/2990/95 dated August 8, 1995 all the stock exchanges had to set up surveillance departments and the exchanges had reported that independent surveillance departments were set up. Since two months have elapsed since the setting up of the Department, we would be interested in knowing-

1. How the department is functioning.
2. What is the present staff strength of the department.
3. The exact nature of market monitoring and surveillance activities

undertaken.
4. The results of the activities in specific terms.
5. How your propose to strengthen this department.

There is no need to repeat that we attach utmost importance to the activity of the market monitoring and market surveillance for ensuring integrity and transparency of the market, which is essential for building up investor confidence.

Further we had sent formats for furnishing various monitoring reports. The stock exchanges which have not started sending these report are advised to do so forthwith. It is reiterated that the Executive Director would be directly responsible for the proper and independent functioning of the surveillance department in the stock exchanges and also forwarding the reports in the prescribed formats to SEBI.

A third circular was issued on May 25, 2000. This circular was issued after the meeting of the Inter-Exchange Market Surveillance Group (ISG) held on May 17,2000. Paras 2 and 3 of the said circular considered relevant in the present context read as follows:

> **2. "The role of Governing Board vis-a vis surveillance functioning of the exchanges-**
>
> **The issue of the role of the Governing Board with regard to surveillance functioning of the exchange was discussed and it was clarified that there is no ambiguity as regards the overall role of the Governing Boards. In this context reference was drawn to earlier SEBI circular no. SMD/3953/96 dated August 17, 1995 wherein SEBI had infact directed the Governing Boards of the exchanges to review the functioning of their surveillance department at every Board meeting.**
>
> **As regards the responsibility of the Executive Director, since surveillance is a very important and sensitive area it was stipulated that this would be under the direct responsibility of the Executive Director who is the senior most executive of the exchange. It was also advised earlier that there should be no interference in the functioning of the surveillance department, which should be done in a very professional and objective manner. The spirit behind such stipulation was that there should be no interference from individual directors, member brokers or any other vested interest and there was never any doubt that Board as a whole would oversee and give policy directive to the surveillance functioning in the exchange.**
>
> **3. Documentation of Surveillance activities: There has to be a proper and systematic documentation of surveillance procedures to ensure transparency, objectivity and accountability in the functioning of the surveillance department. It was agreed that the exchange would put in place a system of documenting surveillance activities within one month."**

Shri Chinoy had placed considerable reliance on the statement in para 1.1 of the circular of August 8, 1995 to show that the responsibility to detect manipulations and monitoring various aspects is cast on the stock exchanges. He had also cited the requirements in sub paras (i), (ii) and (iii) of para 1.3 (b) of the said circular. According to him it is unthinkable of a situation where the exchange can take action without the relevant material before it and the source of the relevant material for this purpose is the Surveillance Department, the exchange management is by the Governing Board and since the Governing Board's powers in an emergency are exercisable by the President he is entitled to have access to the Surveillance Department. In this connection he had cited several provisions from BSE's rules and in particular rule 152 and 154 (a). Rule 152 captioned "special power" under the heading "President and Vice President-Chairman" reads as under:

> **"Rule 152: The President and the Chairman and in the absence of the one, the other shall be entitled to exercise any or all of the powers exercisable by the Governing Board whenever they or he be of the opinion that immediate action is necessary subject to such action being confirmed by the Governing Board within twenty four hours."**

Rule 154(a) captioned "powers vested in Chairman" reads as under:

> **"Rule 154(a): Whenever a Chairman is appointed the powers, rights, duties and functions of the President as provided in the Rules, Bye-laws and Regulations of the**

Exchange save and except those contained in Rules 71(a), 73(a), 81,110,111(a), 111(b), 120(vii), 120(ix), 126(a), 126(b), 127, 131, 132(a), 134(b), 135(c), 136, 148, 150(a), 150 (b), 151, 152 and 153 shall vest in and shall be deemed to be the powers, rights, duties and functions of the Chairman."

Shri Chinoy's submission is that rule 152 is a special power and it remains unaffected by the provisions of rule 154. But according to the learned Advocate General, the special powers to meet emergencies are provided in Bye-laws 71 / 73 and these powers of the Governing Board are vested in the Executive Director and not in the President. These Bye-laws are as under:

Bye-laws:

71. Measures to meet emergencies:

If in the opinion of the Governing Board an emergency exists or has arisen or is likely to occur or if in its opinion the conditions are such as to make free trading in securities extremely difficult the Governing Board may by a special resolution take such action as it deems fit for stabilising the market. Without any way limiting or derogating from the generality of this provision the Governing Board may proceed in such cases in the manner hereinafter provided."

72. xxxxxxxxxxxxxxxxxx

73 (a) In a crisis or in the case of a panic or bear raid or of reckless heavy sales or when it appears that prices are unduly depressed or that a crisis is at hand or that a fair or normal market does not or may not exist the Governing Board may by a special resolution for such period of periods as it may from time to time determine which period or periods shall not except with the approval of the Central Government at any time continuously exceed three days

(i) prohibit short selling in any security or securities; and/or

(ii) fix minimum prices below which sale or purchase of any security or securities shall not be made; and/or

(iii) close the market in whole or in part; and/or

(iv) prohibit further dealings in any security or securities while allowing dealings for closing out or liquidation of existing contracts in such security or securities subject to such restrictions as it may from time to time determine notwithstanding anything to the contrary contained in these Bye-laws and Regulations

Provided that when information regarding prohibition of short selling or fixing of minimum prices or closure of the market or prohibition of further dealings is so conveyed as to reach the Central Government in the normal course within twenty four hours the Governing Board may prohibit selling or fix minimum prices or close the market or prohibit further dealings as aforesaid for any period exceeding three days without the approval of the Central Government till such time as the decision of the Central Government is communicated to the Exchange."

According to the Learned Advocate General these powers are exercisable only by the Executive Director as per the provisions of rule 154 (a) as the said rule does not exclude any of the powers exercisable under any Bye-law. He had further stated that even if it is assumed that rule 152 is a special power to take immediate action, it was not available to the President in the facts of the case as the power has to be normally exercised by the President and the Executive Director jointly and only in the absence of one, the other can independently exercise the power. The fact that the Executive Director was not present in the office at a particular point of time, does not mean that he was not available to discharge the functions, that in the instant case Shri Rathi knew that the Executive Director was available in the Respondent's office at 3.00 p.m. on March 2, 2001. I am inclined to agree with the learned Advocate General that the Rule 152 was not available to Shri Rathi as he claims.

It is necessary to understand the whole purpose of setting up the Surveillance Department and to see whose activities are required to be monitored. For this, one need not have to go beyond the circulars issued by the Respondent cited above. In para 1.1 of the circular dated August 8, 1995 it has been clearly stated that it is the responsibility of the stock exchanges to detect market manipulation like price rigging etc., and to monitor abnormal price and volume movements which are non-consistent with normal trading pattern. The circular further states that it is also the responsibility of the stock exchanges to monitor broker positions, margins, trading limits etc. to ensure that the brokers do not commit defaults adversely affecting the market and the interest of the investors. It has been further stated in para 1.3 that the Surveillance Department should be a separate department entirely devoted to carry out the functions specified in the circular and that the department shall not be saddled with any other responsibility and the department will be directly under the Executive Director of the stock exchange or senior most official of the stock exchange in his absence. Thus on a perusal of the said circular it is clear that surveillance is on the trading activities of the brokers to detect market manipulations so as to take immediate corrective remedial measures. The fact that the department has been carved out and kept as a separate department and put directly under the Executive Director is meant to immunise the department from the reach of the brokers. As the Governing Board of the exchanges have a very large representation of the Brokers and the President is elected from the elected representatives of the brokers, it appears to be a deliberate decision by the Respondent to keep the President and the Governing Board away from the Surveillance Department, and to put the department directly under the Executive Director. An executive Director is a "neutral character" as he is barred from engaging himself in any business during his tenure. Rule 98 is very clear in this regard stating that "the person appointed as Executive Director shall not engage himself in any business directly or indirectly during his tenure of office and if he is a member of the exchange at the time of appointment he shall resign his membership forthwith". The rule further states that "The Executive Director shall be an ex-officio member of the Governing Board and of any committee appointed by the Governing Board of the exchange. Subject to the over all management of the affairs of the exchange being vested in the Board as provided in these Rules, Bye-laws and Regulations the Executive Director shall be vested with the executive powers of the exchange to run the day to day administration and to enforce the Rules, Bye laws and Regulations of the exchange……". In the light of the rule position as stated above and the provisions of Bye-laws 71 to 73 already extracted above, it is clear that the Governing Board or the President is not entitled to contact the Surveillance Department as it is out of their boundary, for the well stated reasons. The fact, that President himself has trading interest and that he is a broker should not be forgotten. Precisely it is for the said reasons that the Surveillance Department is immunised and structured independent of the control of the Governing Board. As the rule 98 clearly states, the Surveillance Department being an outfit in the stock exchange comes under the overall management of the Governing Board, but it is the Executive Director who is vested with the power to run the day to day administration of the said department. In this context it is also to be noted in para 1.4 of the circular under reference timely reporting is to be made to SEBI. The circular does not talk of any such reporting to the Governing Board. It is to be further noted that in terms of clause 13 (b) (i) & (ii), the Surveillance Department is required to monitor price movement of scrips and volume traded and in the event of any abnormalities highlight such abnormality to enable the stock exchange management to take effective action. In the light of rules / provisions explained above, it is clear that the stock exchange management referred to herein is the Executive Director and not the Governing Board or the President. In this context it is also to be noted that in the 2nd circular dated December 6, 1995 also the Respondent had re-iterated that the Surveillance Department should be independent and the Executive Director would be directly responsible for the proper and independent functioning of the department. The word independent used therein is of significance. The role of the Governing Board vis-à-vis surveillance functioning has been well explained in paras 2 and 3 of the third circular of March 25, 2000 leaving no scope for any doubt. It has been stated therein that "there is no ambiguity as regards the overall role of the Governing Boards", that in its circular dated August 17, 1995 the Respondent" had in fact directed the Governing Bard to review the functioning of their surveillance department at every board meeting". "Reviewing the functioning" is an assessment process and not an access process. The circular in the following words has clearly set out the position, that "as regards the responsibility of the Executive Director, since surveillance is a very important and sensitive area it was stipulated that this would be under the direct responsibility of the Executive Director who is the senior most executive of the exchange. It was also advised earlier that there should be no interference in the functioning of the surveillance department, which should be done in a very professional and objective manner. The spirit behind such stipulation was that there should be no interference from individual directors, member brokers or any other vested interests and there was never any doubt that Board as a whole

would oversee and give policy directive to surveillance functioning in the exchange". In the light of the clear cut prohibition on "individual directors, member brokers or any other vested interests, how a member broker President becomes entitled to access the Surveillance Department? Shri Chinoy's emphasis on the direction in the circular that "the Governing Board would oversee and give policy direction to the Surveillance Department" to establish that the President is entitled to have access to the data from the Surveillance Department is unacceptable, as accepting the said proposition would go against the very purpose of setting up a separate and independent department to monitor the activities of the brokers. It would have been easy to accept Shri Chinoy's proposition, had the Governing Board been a 'broker minus' set up, but that is not so in BSE today. The President does not cease to be a member broker the moment he becomes President. Neither the other broker directors. On the contrary the President will cease to be so the moment he ceases to be a member broker as his election itself to the Governing Board is based on the said qualification. In the present set up, brokers are the umpires and also the players. In fact even as of now the stock exchanges (barring NSE) are of the brokers, for the brokers and run by the brokers. In such a set up, it is difficult to accept the version that the Governing Board should have access to the surveillance data. Thus it is clear that even though the Governing Board is empowered to oversee and give policy directions to the Surveillance Department certainly it is not empowered to interfere with the day to day functioning of the department.

Shri Chinoy had referred to a press release issued by the Respondent on January 17, 2001 reporting the decisions taken during the SEBI convened meeting of all the stock exchanges on January 17, that one of the decisions taken therein was that "the directors and the functionaries shall refrain from acquiring information other than as may be necessary for discharging their duties. Proper audit trail, prescribed channels and confidentiality of information would be maintained at all point of times". He stated that Shri Rathi had obtained the information for discharging his duties. In this context the requirement of collecting the information through prescribed channel cannot be glossed over. If any action is required to be taken at the Board level the requisite information would be supplied by the Executive Director and he in turn is expected to filter the information and hold back the information which are likely to be used by someone to his advantage or to the detriment of others and the market. There is not even a suggestion in the said press release referred to by Shri Chinoy that a broker director who by virtue of his official position is entitled to obtain information having bearing on the trading, over others. In fact Shri Joshi, the Executive Director of BSE in his statement before the investigating officer had stated that "there is no interaction with Shri Rathi on daily basis on surveillance matters, which are discussed in the sub group appointed by the Governing Board". This is the normal practice. He had also stated that "I also enquire if there is a sudden spurt or dip in the sensex and the reasons thereof. In case of abnormal situation I call up the officer concerned, who monitors the broker positions to know if there are any abnormal positions of any member in any scrip. I approve all surveillance issues pertaining to reduction of circuit filters, imposition of special margins". Shri Rathi cannot be unaware of this practice. Shri Rathi in his deposition before the investigating officer had also stated that "the Governing Board has the over all responsibility of overseeing the functioning of the surveillance department. I am not aware of any decisions of the Governing Board prohibiting access of any information from surveillance department by the President. In fact as mentioned earlier when the surveillance committee meetings are held, lot of information is presented and given by Executive Director, General manager (surveillance) and other surveillance staff in respect of the matters, which are discussed in such meetings and based on such information and discussions decisions are taken in the surveillance meetings. It may please be noted that for taking any decision, policy or otherwise the flow of information is a prerequisite". What Shri Rathi stated is the correct procedure. His statement shows that the Board was getting those particulars required for taking policy decisions from the proper channel and not directly from the Surveillance Department. He had further stated that "such information is also required in exceptional circumstances such as those existed on March 2, 2001. The information and relevant feed back is usually made available in such circumstances by the Executive Director or senior executives of the exchange.

However, in the instant case since these executives were not available, my secretary connected me to Mr. Dhanawade, when I asked her to connect me to the next person incharge". In this context it is to be noted that Shri Rathi was well aware that the Executive Director and General Manager were in the Respondent's office, not far away from BSE, and also that they were available on mobile telephone. Further it was 3.10 PM and the usual exchange closing time was 3.30 p.m. and the following next two days being Saturday and Sunday the market would remain closed. There was no urgency to collect the information, in the manner as Shri Rathi did, at that point of time to "exercise the Governing Board's over all

responsibility of overseeing the functioning of the Surveillance Department". He could have very well waited for the Executive Director and General Manager to be back in office, or should have contacted them on their mobile phone, but still he ventured to obtain information in breach of the Respondent's directions. In this context, his another submission is also noteworthy. He had told the investigating officer that "I have not obtained any information directly from the surveillance department in the past. However, in case of any unusual movements in the market I had received queries from Finance Ministry and Regulators to find out broad reasons for unusual movements and particularly the behaviour of the Financial Institutions, etc. Normally such calls were received by the President only. Such unusual movements in the markets require initiation of action for the purpose of risk management, safety and integrity of the market. In such unusual circumstances communications were made with the Administration". Thus shri Rathi admits that in the past to find out broad reasons for unusual movements, he, in discharge of his duties used to communicate with the "administration" and not directly with the Surveillance Department as he did on March 2. The statement of Shri Rathi that he had not contacted the Surveillance Department in the past is corroborated by Shri P.S.Reddy, General Manager (Surveillance) before SEBI.. To the question that "do you know / have any other sound recording except that of March 2, 2001 in which the President of the stock exchange, Mumbai Shri Anand Rathi is seeking information pertaining to scrips and the position of various members in particular scrips? Please confirm the same and comment"; Shri Reddy in answer stated that "to the best of my knowledge Shri Anand Rathi have never asked me for any such information till date. I listen to voice recording system approximately once in two months and listen to few calls randomly. I have never come across any call made by Shri Anand Rathi asking for any of the aforesaid information. Further none of the employees have also informed me the happening of any such incidence in my absence as they did on March 2, 2001". He had reiterated this view to another question by saying that "Shri Anand Rathi has never asked information which includes scrip specific and member specific". To another question as to what is his level of interaction with the President (Shri Rathi) in matters relating to surveillance Shri Reddy had stated that "the Governing Board has constituted a committee comprising of the Executive Director, the RBI nominee, Public Representative and Shri Himanshu Kazi. The said committee is headed by Shri Anand Rathi in his capacity as President of the exchange. The committee takes only decisions pertaining to policy issues involved in the matter of surveillance at the exchange. No specific individual or case to case decisions are taken, or discussed at the meeting". This statement clearly indicates how the exchange did really understand its role and the manner in which the Governing Board was overseeing and giving policy directives to the Surveillance Department in terms of the circular. Shri Joshi's reaction after listening to the tape was that "I was shocked that such conversation has taken place". There is nothing on record to show that Shri Rathi had discussed about any measures with the Executive Director or General Manager on their return to the exchange. The response of the Executive Director on hearing that "the President was enquiring about few index counters and the positions of brokers in scrips I immediately expressed my deep displeasure with Shri Dhanawade", indicates the wrong doing by the President. Shri Tirodkar, Director in charge of the Surveillance Department has gone on record before the investigating officer stating that " Shri Rathi has not asked any specific information during his term as President". But on March 2, 2001 it was not so.

From the facts and circumstances explained above it is clear that Shri Rathi had directly obtained information from the Surveillance Department and that obtaining information from the Surveillance Department by Shri Rathi was in violation of the directions contained in the three circulars referred to above.

Shri Chinoy had argued that the circulars under reference are only advisory and not legally enforceable. In this context it has to be noted that the said circulars were issued for the purposes of the Act. The purposes of the act are discernible from the preamble of the Act wherein it has been stated that "it is an act to provide for the establishment of a Board to protect the interests of investors in securities and to promote the development of, and to regulate, the securities market and for matters connected therewith or incidental thereto". As per Section 11of the Act it is the duty of the Respondent to achieve the said object by such measures as it thinks fit. Division Bench of the Hon'ble Gujarat High Court in Alka Synthetics v. SEBI (1999) 19 SCL 461 has explained the scope of the expression "measures" stated in the section.

> **"The SEBI Act is an Act of remedial nature and, therefore, the preset cases could not be compared with the cases relating to the fiscal or taxing statutes or other penal Statutes for the purposes of collection of levy, taxes etc. As and when new problems arise, they call for new solutions and the whole context in which the SEBI had to take a**

decision, on the basis of which impugned orders were passed, cannot be said to be without authority of law in face of the provisions contained in section 11 and section 11B. As the language of section 11(1) itself shows and as the matters for which the measures can be taken are provided in sub-section (2) of section 11. It is clearly made out by the plain reading of the language of the section itself that the SEBI has to protect the interests of the investors in Securities and has to regulate the securities market by such measures as it thinks fit and such measures may be for any or all of the matters provided in sub-section (2) of section 11 and in due discharge of this duty cast upon the SEBI as a part of its statutory function, it has been invested with the powers to issue directions under section 11B. ……. Thus, so far as the authority of law in the SEBI to issue such directions is concerned, such authority to take measures as it thinks fit is clearly discernible on the basis of the provisions contained in section 11 read with section 11B of the SEBI Act. We have to therefore consider and interpret the power of SEBI under the provisions so as to see that the objects sought to be achieved by Act is fully served, rather than being defeated on the basis of any technicality…… The duty and function had been entrusted to take such measures as it think fit and in order to discharge this duty, the power is vested under section 11B. ……. The authority has been given under the law to take appropriate measures as it thinks fit and that by itself is sufficient to cloth the SEBI with the authority of law".

The circulars issued by the Respondent contain the measures to protect the interest of the investors in securities and the securities market. These circulars are therefore enforceable.

The Appellant's version that he had not acted surreptitiously, but in a transparent manner as the call was put through his Private secretary and in the presence of six others in fact goes against him. Knowing very well that the surveillance information is a confidential information, obtaining the same that too in the presence of others is not a matter to be treated as an indication of the Appellant's bonafides. Further the claim that the Appellant was aware of the built in voice recording system as he was instrumental in installing the same is also of little help as he knew that the recorded conversations are not normally replayed and examined routinely. The recorded conversations are not scrutinised on a day to day basis is evident from Shri Reddy's statement that "I listen to voice recording system approximately once in two months and listen to few calls randomly". So it was a safe bet. The submission that the Appellant himself had written to the Respondent on February 7, 2001 requesting to order inquiry into the matter is also of not much help to him. Shri Joshi in his statement dated March 31, 2001 had stated that –" March 6th was a holiday and the General Manager (surveillance) informed me on phone at my residence that officials from SEBI had come to the exchange to listen to the recorded conversation. Around 4 p.m. I went to the office and nothing could be done on that day in this regard. On 7th I got a call from Shri L.K.Singhvi, Senior Executive Director, SEBI to meet in his office at 11 am along with General Manager (surveillance) and instructed me to make available a copy to SEBI". Shri Rathi being the President of BSE at that point of time cannot be unaware of the fact that the SEBI had already seized of the matter and an inquiry was imminent. Therefore his letter dated February 7, 2001 to SEBI asking to conduct an inquiry, appears to be more for record purpose than for anything else.

The next question to be considered is as to whether the information obtained by the Appellant from the Surveillance Department is price sensitive or not. Since the Respondent has given the benefit of doubt to the Appellant in the matter of violation of the provisions of the Insider Trading Regulations and the UTP Regulations and in the light of the finding that there was no evidence of using the information, the question whether the information so obtained was price sensitive or not has lost much of its significance. However, since there is an allegation that the information received is price sensitive in nature and the same was obtained to benefit his broking entities, it is felt necessary to have a look at the information obtained by Shri Rathi from Shri Dhanawade. The Respondent has viewed that the information obtained by Shri Rathi is price sensitive. Shri Reddy, General manager (Surveillance) to a pointed question by the Investigating officer that " do you consider the information sought by Shri Anand Rathi is price sensitive in nature or not had answered in the affirmative – that "Yes the information sought by Shri Anand Rathi is price sensitive. Further the information is not price sensitive the same would have been displayed to all the members". Shri S.T.Garella another senior functionary in the Surveillance Department of BSE in his statement with reference to the investigating officer's query relating to the information passed on by Shri Dhanawade on the position of members in the scrip of Infosys, Reliance, Satyam, Himachal, had stated that "the information is price sensitive in nature which could affect the trend of the market". In this context it has also to be noted that if the information given by Shri Dhanawade was insensitive,

there was no cause for the Executive Director to "feel shocked" on hearing that Shri Rathi had contacted Shri Dhanawade and obtained certain information. In any case, as the transcript of the conversation is available let us have a look at the information, obtained by Shri Rathi from Shri Arun Dhanawade. For easy reference purpose I have put serial numbers to the questions:

Srl.No.

1. "Secretary Hello! Hello! Mr. Rathi will speak to you. Your awaj (voice is not very clear Mr. Arun Regarding what? What happened?

2. Secretary I wouldn't know yaar. He asked for Mr. Reddy. Mr. Reddy is gone to SEBI, so he said give me the next person. Be on the line, one second

Then the secretary transferred the line and phone was out on music.

In the background Mr. Arun was speaking to somebody saying that Shri Rathi kas phone hai.

3. Mr. Rathi Hello! Hello!
Mr. Arun Yes Sir!

4. Mr. Rathi Arun wo aah gaaye kya, Reddy?
Mr. Arun Reddy saab SEBI mae hai

5. Mr. Rathi Swo nikal gaaye, ateh he mere baat karana, per thab ye jo teen, char counter me particularly jo index mae, jisme kaam ho raha hai, usme kya koi institutional selling hai kya?
Mr. Arun Basically operators are only selling

6. Mr. Rathi Acha
Mr. Arun In the morning there was lot of institutional were selling, only Credit Suisse was selling heavily

7. Mr. Rathi Credit Suisse ne beccha hai?
Mr. Arun Credit Suisse ne baecha hai

8. Mr. Rathi Kiske behalf se baecha hoga.
Mr. Arun Wo tho I will get the client details. Basically FII karke mark karte hai

9. Mr. Rathi Acha aur kiske sale jaada thi
Mr. Arun Himachal mae main dekthan hoon

10. Mr. Rathi Aur?
Mr.Arun Himachal mae main dekthan hoon

11 Mr. Rathi Nai nai Credit Suisse ke alawa aur kiske broker ke sale thay jaada?
Mr. Arun Turnover wise

12. Mr. Rathi Ah, sale kiske jaada hai, Kounse broker ke, FII broker ke
Mr. Arun I will just check one minute sir.
Mr. Arun I am just refreshing it, one moment

In the background, phone was ringing

13. Mr. Rathi hello!
Mr. Arun Just a minute

14 Mr. Rathi Ek minute

On the Background Mr. Rathi was attending another call

Mr. Arun Hello!Hello! Sir

15. Mr. Rathi Ha
Mr. Arun Basically in Himachal and all, basically operators are only acted basically Mr. Arun Most of the sellers are operators only. We don't find much of institution one or two were there. Only one or two or there about institution, credit rest all are not institutional

16. Mr. Rathi Credit Suisse only
Mr. Arun But rest all of we find is all operators only, basically Operators are selling

17 Mr. Rathi Aur Aur kya huwa? Aur basically isme

18 Mr. Rathi Infosys wagere mein kya?
Mr.Arun Infosys also basically operators are only sold it sir
Mr. Arun Last day this is basically Friday so they must have squared it up or something we don't find much of FIII seen over here at least

19 Mr. Rathi No Infysys, usme nahi hai, FII ka nahi hai Insofys me?

20 Mr. Rathi Aur satyam mein?
Mr. Arun Third hai. Third Credit Suisse hai. Infosys selling only we find Credit Suisse is there. Baki sab operators he hain, Morgan is also there

21 Mr. Rathi Morgan hai?
Mr. Arun Yes Sir

22 Mr. Rathi Aur kaun hai? First two names kya hai?
Mr. Arun First two names hai Kotak hai, Ramraj hai

23 Mr. Rathi Kaun hai ye
Mr.Arun Ramraj Securities in Infosys Si, Kotak, Ramraj then Credit then Maheshwari then CD Equisearch and then J M Morgan

24 Mr Rathi J M Morgan
Mr Arun i.e. out of the top five, top six two are

25 Mr Rathi Kotak tho institution he hoga na?
Mr Arun Kotak ka tho I will just check up the trades
Mr Arun Kotak is having a quite bit of institution

26 Mr Rathi Institution he hoga na? OK
Mr Arun Then in Satyam also we are having mostly operators Sir

27 Mr Rathi Acha koi institutions nahi hai
Mr Arun JM Morgan hai Sir, Last mein hain

28 Mr Rathi Baki uper kaun hai
Mr Arun Baki uper hai Damani hai, Bakliwal hai, Damani Share?

29 Mr Rathi Which which?
Mr Arun Damani shares damani shares and stockbroker 595

30 Mr Rathi Ye kaun hai?

31 Mr Rathi Acha OK aur
Mr Arun Aur baki LK Pande, LK Pandey, he also must be having some institutional trades

32 Mr Rathi OK
Mr Arun Uske baad mein hai Reliance Sir, Reliance mein be top sellers hain here also Morgan is there, Jardine is there, Dresdner is there. There are lot of

institutionals are there

33 Mr Rathi Kisme?
Mr Arun Isme hai! Reliance mein seller be kafi hain Sir, Badme Wipro main, Wipro main jaada Ind. Suez is on the 5th place. Baki sab operators he hain.

34 Mr Rathi Tick hai
Mr Arun Global Tele, Global Tele usme kafi institution nai, Ek do hai institution

35 Mr Rathi Hai
Mr Arun Claridges hai

36 Mr Rathi Kaun hai?

37 Mr Rathi Bearing
Mr Arun Claridges, Claridge 190

38 Mr Rathi OK
Mr Arun Baki operators he hai Sir. Spread out only Mukesh Babu is highest Sir, I suppose 450

39 Mr Rathi OK
Mr Arun I don't think institution any way I will check up and let you know

40 Mr Rathi Acha OK Reddy aate hei baat karana
Mr Arun Yes Sir"

(Shri Chinoy had pointed out slight discrepancies in the transcript , which are not materially of that important for the purpose for which the above conversation is extracted).

Though the Appellant had stated that there was an emergency and that is why he contacted Shri Dhanawade, a junior functionary in the Surveillance Department, without waiting for the Executive Director and General Manager to come, it is seen from the recorded timing in the transcript that the conversation went on for 5 minutes and 25 seconds from 15:10:35hrs. I do not see from the manner in which the conversation was going on as per the transcript there was any urgency on the part of Shri Rathi, to obtain information to meet an emergent situation or the conversation was confined only to sales by FIIs. If the Appellant was concerned only about the role of the institutional sellers he could have cut short the talk on hearing Dhanawade's reply to question 5. But the conversation was stretched. Questions 8, 9, 11, 12, 16, 17, 18, 20, 21, 22, 23, 24, 25, 28, 30, 33, 36, 37 and 38 are specific to certain scrips and brokers. Trading details in particular scrips cannot be considered as not price sensitive particularly in the volatile market conditions.

The observation of the Respondent based on its experience as market regulator that "the mere knowledge of the fact that the institutions are buyers or sellers in certain scrips would give clear indication of trends to any person on the price movement in the scrip. Therefore this information is extremely price sensitive and anyone who has knowledge of the same has an unfair advantage over other market players" has also to be given due weightage. In the light of the conversation as reflected in the transcripts and also the unanimous view of Shri Reddy, Shri Tirodkar, and the Respondent stated above I am convinced that the information obtained by Shri Rathi from Shri Dhanawade on March 2, 2001 was price sensitive at that point of time. It is of not much relevance to find out as to whether the information obtained come under the definition of the expression "unpublished price sensitive information" as defined in the Insider Regulations but certainly the information was price sensitive from the trading angle. However as per the impugned order though the information was price sensitive, the Appellants did not make use of them. In any case in my view the information obtained by Shri Rathi was not information, which as he claimed required for any crisis management.

Having come to the conclusion that Shri Rathi had obtained price sensitive information from the Surveillance Department, in breach of the governing directions in position and that the information was price sensitive in nature, the next question is on the legality of the order made by the Respondent against the Appellants. Since the order is mainly based on the findings and the recommendations of the Enquiry Officer, it is worth having a look at the same as recorded in the impugned order. Extracts of the findings as it appears in the order are as

under:

Para 3.1

(a) Shri Rathi obtained information from the Surveillance Department at about 1510 hrs on 2nd March 2001

(b) By seeking such information, Shri Rathi had contravened the provisions of three circulars of SEBI and interfered with the functioning of the Surveillance Department;

(c) The information obtained by Shri Rathi was price sensitive in nature;

(d) Such information was actually taken for the benefit of his broking entities;

(e) Seeking of such information amounted to misuse of his position as broker-director of broking entity and as President of the Exchange. He had no authority whatsoever to obtain such information;

(f) The fact that Shri Anand Rathi, broker-director and President of BSE sought price sensitive information from the Surveillance Department eroded the confidence of investors in the fair, transparent and impartial working of stock exchanges in particular and securities market in general;

(g) By obtaining such information from the Surveillance Department, Shri Rathi failed to act with the integrity and, thus, violated Code of Conduct as broker-director and ceased to be a "fit and proper" person under SEBI Regulations. Therefore, the entities in which he was a director of which were under his control ipso facto ceased to be "fit and proper" bodies;

(h) Though the information was unpublished and price sensitive and Shri Rathi could be considered as an insider, there was inadequate evidence in the preliminary investigation report to prove a violation of SEBI (Insider Trading) Regulations, 1992 by Shri Rathi or his associate entities;

(i) After considering the preliminary investigation report and the explanation of the noticees, Shri Rathi and his associate entities were given the benefit of doubt on the point of the use of information by them to make unlawful gains or to avoid loss to attract SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995;

(j) Penalty could be imposed on a corporate entity for the violations committed by an individual director associated with the corporate entity especially if that entity was a broking entity.

The Enquiry Officer made the following recommendations:

Para 4.1:

(a) Anand Rathi Securities Pvt.Ltd, Rathi Global Finance Ltd. and Rathi Capital & Securities Pvt.Ltd were guilty of violation of Code of Conduct (i.e. failed to act with integrity, compliance with statutory requirements) and Regulations pertaining to "fit and proper" person. The Enquiry officer recommended that a penalty of suspension of registration under Regulation 28 of SEBI (StockBrokers and Sub-brokers) Regulations, 1992 and Regulation 34 of SEBI (Portfolio Managers) Regulations, 1993 for a period of 9 (nine) months should be imposed. Further, since the above mentioned entities had already been restrained from carrying on their broking /sub-broking activities from March 12, 2001, it would be just and fair to adjust the proposed period of 9(nine) months while imposing the penalty of suspension.

(b) No penalty was recommended to be imposed on Navaratan Capital & Securities Pvt.ltd, which was under the control of the Gupta family and not under the Rathi family

(c) It would be appropriate in the interest of the securities market that Shri Rathi should be restrained under section 11 and section 11B of the SEBI Act, 1992, from being associated with any of the capital market related institutions /entities for a period of 2(two) years. While reckoning the above-mentioned period, the period of operation of SEBI order dated the 12th March 2001 could be adjusted.

It is seen from the impugned order that Shri Rathi has been restrained from holding any position of director trustee of any capital market related institution /entities for a period of two years from March 12, 2001. The said direction has been issued under section 11 and 11B of the Act. This direction is in the light of the finding that Shri Rathi had obtained information from the surveillance department in breach of the three circulars governing the surveillance activities of the exchanges which seek to prohibit any interference with surveillance from the elected directors. The Respondent's version as recorded in the order in this regard is as under:

"We have carefully considered the findings and the recommendations of the Enquiry Officer, the reply of Shri Anand Rathi and its associate entities and also the submissions made at the hearing by the counsels of Shri Anand Rathi and its associates during the course of hearing and subsequent written submissions. We now proceed to deal with the issues as under:

Factual conclusion – We find that Shri Rathi has not disputed that he had got information from Shri Arun Dhanawade, an officer of the Surveillance Department of BSE, on the 2nd March, 2001 during the trading hours at 1510 hrs, in respect of position of certain brokers / Foreign institutional investors and scrips. This information was with reference to some momentum scrips such as Infosys, Satyam etc. However, he disputed that the said information which he got was price sensitive, malafide or amounted to interference with the functioning of the Surveillance Department of the Stock Exchange. Shri Rathi further contended that he sought this information in the presence of six brokers of which 3 were elected directors. The call was put through by his secretary. He was also aware that his conversation would be recorded as he himself was instrumental in getting the voice recording system installed.

8.3: Rules and Bye-laws of BSE – Shri Rathi contended that as a President of BSE he was duty bound and specifically authorised to act as such in the given circumstances. He relied on the provisions of bye-law 73(a) rule 118, 148, 152, bye-laws 4,6 & 60 of the BSE to buttress the argument that it was within the power of the President to seek such information. He further contended that his conduct was not in violation of the three circulars issued by SEBI".

The Respondent after considering the scope of the rules and bye-laws referred to by Shri Rathi concluded that the President did not enjoy any such power as claimed by the Appellant, to obtain the information from the Surveillance Department.

With reference to the circulars the Respondent had viewed that, it agreed with the finding of the Enquiry Officer that Shri Rathi while seeking such information had contravened the provisions of the three circulars and his act amounted to interference with the functioning of the surveillance department.

As far as the other two Appellants are concerned their registration was suspended for nine months, under regulation 26 of the Stockbrokers Regulations. The Respondent has stated the reasons for the same in para 10.1 of the order, which we will examine later.

The Respondent summed up its finding in para 13.4 of the order as follows: -

"We have come to the findings in the preceding paragraphs that Shri Rathi has violated the provisions of the above three circulars and also interfered with the functioning of the Surveillance Department. We have also concluded that the same amounted to violation of Code of Conduct in respect of failure to comply with the statutory requirements and also failure to maintain integrity. We are in agreement with the findings of the Enquiry Officer that the above has shaken the confidence of investors in the transparent, impartial and independent functioning of the Stock Exchanges. We have also come to the finding that Shri Anand Rathi and two of his broking entities, namely, Anand Rathi

Securities Pvt.Ltd and Anand Rathi Direct India Pvt. Ltd violated the requirement of "fit and proper" criterion under the SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992."

The Respondent has invoked the provisions of section 11 and 11B of the Act. Section 11(1), which is general in nature reads as under: -

"11. (1) Subject to the provisions of this Act, it shall be the duty of the Board to protect the interests of investors in securities and to promote the development of, and to regulate the securities market, by such measures as it think fit.

Section 11(2) is on certain specific measures which the Respondent is empowered to take.

Section 11B is on the Respondent's power to issue directions, which is as follows: -

Save as otherwise provided in section 11, if after making or causing to be made an enquiry, the Board is satisfied that it is necessary; -

(i) in the interest of investors, or orderly development of securities market; or

(ii) to prevent the affairs of any intermediary or other persons referred to in section 12 being conducted in a manner detrimental to the interest of investors or securities market; or

(iii) to secure the proper management of any such intermediary or person.

it may issue such directions,-

(a) to any person or class of persons referred to in section 12, or associated with the securities market; or

(b) to any company in respect of matters specified in section 11A, as may be appropriate in the interests of investors in securities and the securities market"

One has to view the powers of the Respondent under the provisions of the Act in the context of the objects sought to be achieved by the Act and the duty cast on the Respondent in achieving the same. Section 11 and section 11B give enormous authority to the Respondent in this regard. As long as the power exercised under section 11B is subject to the provisions of the Act and well within the legal and constitutional frame work, intended to achieve the purposes of the Act and subjecting the persons specified in the section, the power will sustain.

This Tribunal had examined in detail the scope and reach of the section 11 and 11B in Bank of Baroda v. SEBI (2000) 26 SCL 532: (2000) 38 CLA 226 and held:

"Section 11 and section 11B are interconnected and coextensive as both these sections are mainly focussed on investor protection. On a careful perusal of the said section 11 referred to in the earlier paragraphs, it could be seen that the Respondent has been in no uncertain terms mandated to protect the interests of investors in securities by such measures as it thinks fit. Of course those measures are subject to the provisions of the Act. The expression 'measure' has not been defined in the Act. So we have to go by its generally understood meaning. According to Corpus Juris Secundum measure means "anything desired or done with a view to the accomplishment of a purpose, a plan or course of action intended to obtain some object, any course of action proposed or adopted by a Government". However, I am not inclined to agree with the Respondent's view that the power under section 11 is unlimited. I am of the view that the legislature has circumscribed the power, by putting the caveat that these measures are subject to the provisions of the Act. The ambit of power is contained within the framework of the Act. But within the statutory frame work such power reigns.

While section 11 deals with the functions of the Board, section 11B is on the powers of the Board. Section 11B is more action oriented, in a sense it is a functional tool in the hands of the Board. In effect section 11B is one of the executive measures available to

the Respondent to enforce its prime duty of investor protection. As could be seen from the text of the section reproduced above, the Respondent is empowered to issue directions in the interests of investors to any person or class of persons referred to in section 12 of the Act or associated with the securities market. In other words the section identifies the persons to whom and the purposes for which, directions can be issued."

In the light of the above it is clear that the SEBI in terms of section 11 and 11B is entitled to take measures /directions for protecting the interests of the investors and to promote the development of, and to regulate the securities market and for matters connected. It is totally incorrect to say that the Respondent has no power under section 11B to protect the interests of investors in the light of this Tribunal's decision in Sterlite. There is not even a suggestion to the said effect in the Sterlite case. This Tribunal had only held that 11B cannot be invoked for imposing penalty as the section is not intended for the said purpose as could be seen therefrom.

In Sterlite's case (supra), the Tribunal after analysing several authorities had held:

"It is to be noted that the power under section11B is restricted to issue appropriate direction for the purpose of protecting the interest of the investors etc. mentioned in the section. The scope of the expression 'direction' has not been defined in the Act. But the word has been judicially interpreted by Courts. Hon'ble Bombay High Court had viewed that 'in law direction means guidance or command' (AIR 1988 Bombay 416 at p. 421). According to the Hon'ble Supreme Court in Rajendranath v.CIT (1979) 4 SCC 282, "a direction by a statutory authority is in the nature of an order requiring positive compliance". According to Blacks Law Dictionary direction means 'a guiding or authoritative instruction, order, command'.

It has to be noted that section 11B does not even remotely empower the Respondent to impose penalties. Hon'ble Calcutta High Court had held that prescribing an offence and its punishment is an essential plenary function of the legislature (D.N.Ghosh v. Addl. Sessions Judge (AIR 1959 Cal.208.) Hon'ble Gujarat High Court also held the same view in Delux Land Organisers v. State of Gujarat (AIR 1992 Guj. 75) holding that "any power to impose penalty must be statutorily warranted and executive Government cannot create penal provisions by issuing circular when there is no authority to impose such penalty flowing from any provision of law". Hon'ble Supreme Court in Khemka and Co. (Agencies) Pvt.Ltd v. State of Maharashtra (AIR 1975 SC 1549), while considering the question as to whether the assessee under the Central Sales Tax Act, 1956 could be made liable for penalty under the provisions of the State Sales Tax Act, had considered the power to impose penalty. It had held:

"It is well settled canon of construction of statutes that neither a pecuniary liability can be imposed nor an offence created by mere implication. It may be debatable whether a particular procedural provision creates a substantive right or liability. But I do not think that the imposition of pecuniary liability, which takes the form of a penalty or fine for a breach of a legal right can be relegated to the region of mere procedure and machinery for the realization of tax. It is more than that. Such liabilities must be created by clear, unambiguous and express enactment. The language used should leave no serious doubts about its effect so that the persons who are to be subjected to such a liability for the infringement of law are not left in a state of uncertainty as to what their duties or liabilities are. This is an essential requirement of a good government of laws". (emphasis supplied)

The legislature has clearly spelt out the penal provisions in the Act at 3 places – section 12(3) provides for suspension or cancellation of the certificate of registration granted to the market intermediaries in the event of their proven misconduct, provision under Chapter VIA, provides for imposition of monetary penalty for certain offences specified therein; section 24 empowers Courts to award punishment for violation of offences under the Act etc. Since legislature has deliberately chosen to create specific offences and penalties thereto, it is not possible to view that under section 11B the Respondent is competent to issue a direction which tantamounts to imposition of penalties. While widening the scope of 'such measures' used in section 11, to include penalties, and thereby stretching the scope of issuing directions under section 11B to cover imposition of penalties, the limitation stated above need be kept in mind".

I find from the then member of SEBI, Prof. Verma's order dated

March 30, 2001 that he had also viewed that section 11B is not meant for taking punitive action.

> **Prof. Verma had viewed that "in the interest of investors, and the orderly development of securities market, it was and is necessary to restrain Mr. Anand Rathi from acting as a member of the governing board of the exchange. This was and is a matter of great urgency and importance requiring the use of the residuary powers that SEBI enjoys u/s 11B.**
>
> **However, I do not see sufficient justification for the exercise of powers u/s 11B to direct Mr. Anand Rathi and his concerns not to undertake any fresh business as a broker.**
>
> **(a) Whether Mr. Anand Rathi and his concerns act as brokers or not does not make any difference to the governance of the stock exchange and is not therefore of serious consequence to the orderly development of the securities market. Nor am I convinced that the direction is essential in the interest of investors. No case has been made out that these concerns have carried out their broking business in a manner prejudicial to the investor interest.**
>
> **(b) I would like to emphasise the crucial distinction that S 11B is a provision not for punishing intermediaries but for protecting investors and the markets. Therefore, while contemplating an order u/s 11B, we should not be asking ourselves whether a particular individual or entity is deserving of punishment. We should rather ask whether the contemplated direction is necessary in the interests of investors or for orderly development of the securities market.**
>
> **(c) I have already stated that it was totally improper and unacceptable for Mr. Anand Rathi to seek detailed and highly price sensitive information from the surveillance department of the stock exchange.**
>
> **Prima facie, it is possible that this action may warrant punishment under various SEBI regulations:**
>
> **(d) The proper course of action for SEBI to proceed against Mr. Anand Rathi for any of the possible violations of the Insider Trading Regulations and Stock Broker Regulations indicated above is to follow the procedure laid down under those regulations. I think it is inappropriate to avoid these regulatory procedures and attempt to impose the penalty under the grab of a direction u/s 11B.**
>
> **(e) By following the due process of law laid down in the regulations, the regulator would increase its own prestige and dignity and enhance the respect for the rule of law in the securities market. The regulator must not only be fair but must also be seen to be fair.**
>
> **(f) It is not sufficient that the end result of the suspension / cancellation of registration that may follow at the end of due enquiry is materially the same as that achieved by the direction not to undertake fresh business as a broker. It is also necessary that that end result be invested with the nature of a penalty. The order u/s 11B by contrast is a direction "for" investor interest and not an order "against" the alleged violator of the regulations.**

2. For these reasons, I am of the view that:

> **(a) The first part of the order of March 12, 2001 under which Mr. Anand Rathi and his concerns were directed not to undertake any fresh business as a broker is not sustainable and should be vacated forthwith;**
>
> **(b) The second part of the order under which Mr. Anand Rathi was restrained from acting as a director member of the Governing Board of the BSE is necessary in the interest of investor and for orderly development of the securities market and should continue;**

(c) Proceedings must be initiated under Regulation 28 of the Stock Broker Regulations for possible imposition under the regulations".

It is to be noted that the Respondent had conducted enquiries and passed the order under section 11B against Shri Rathi and under the Stockbrokers Regulations against the two Appellant companies.

The Appellant's argument that the Respondent itself had considered the direction under section 11B as punitive and that is why it had vide the show cause notice dated September 27, 2001 called upon the Appellant to show cause as to why penaltiesrecommended by the Enquiry Officer should not be imposed. In this context it has to be noted that the said show cause notice was issued to 5 entities which included Shri Rathi and the Appellant companies. It is a combined notice based on the Enquiry Officer's findings as is stated in the notice itself. In the said notice in respect of Shri Rathi the Enquiry Officer had recommended as follows: -

"In view of the above it is recommended that it would be fit and proper in the interest of securities market that Shri Rathi be restrained under section 11 and 11B of SEBI Act, 1992, from being associated with any of the capital market related institutions /entities for a period of 2 (two) years".

In respect of the two Appellant companies the Enquiry Officer had recommended that:

"In the circumstances and facts of the case, I recommend a penalty of suspension of registration under Regulation 28 of SEBI (Stock Brokers and Sub Brokers) Regulations, 1992 and Regulation 34 of SEBI (Portfolio Managers) Regulations, 1993 for a period of 9 (nine) months on the following entities:

a. Anand Rathi Securities Pvt.Ltd
B. Rathi Global Finance Ltd
c. Rathi Capital & Securities Pvt.Ltd

These entities will not trade in securities and act as brokers/sub-brokers during the period of suspension. They shall also not act as portfolio managers during the suspension period. I am of the opinion that a suspension for a period of 9 (nine) months would be appropriate in their case. It is also observed that these entities have already been restrained from carrying on their broking / sub-broking activities from March 12, 2001. It would therefore would be just and fair to adjust this period also while recommending this penalty."

Thus on a combined reading of the notice with the recommendations of the Enquiry Officer it is clear that there was no proposal to impose any penalty on Shri Rathi, but what was recommended in his case was to restrain him under section 11 and 11B of the Act, from being associated with any of the capital market related institutions/entities for a period of 2 years. Only in the case of associate entities the Enquiry Officer recommended a penalty of suspension under the governing regulations. In these circumstances it is not possible to accept the Appellant's version that the Respondent itself had considered the direction as a penalty.

In R.K.Aggarwal's case the challenge was to the Respondent's order directing Shri Aggarwal, who was the President of UP Stock Exchange, to relinquish the office of the President of Uttar Pradesh Stock Exchange and disqualifying to be a member of the Governing Board or office bearer of the exchange as well as any capital market related institutions for a period of 2 years on the ground that Shri Aggarwal:

(i) had exceeded his authority as Vice President of the exchange by interfering with margin and surveillance system of the exchange

(ii) had failed to initiate any action against the two members of the exchange who had allegedly become members by submitting fake educational certificates.

(iii) walked out of a Board meeting which was chaired by him intentionally with a view to disrupt the proceedings of the meeting to delay decision making in a matter of considerable importance to the exchange.

(iv) got the trading terminal of another broker deactivated / reactivated by unwarrantedly interfering in the surveillance related activities of the exchange.

In Aggarwal's case, in the order the Chairman of the Respondent had viewed that "the conduct of the President of UPSE, Mr. R. K. Agarwal has put serious questions on the transparency and integrity of the system. This has also created an adverse public perception, which is harmful to the confidence of the investors and the market". He had further viewed that "all these actions of Mr. R. K. Agarwal raise serious issues of propriety and credibility and his conduct has been found to be unbecoming of a head of the organisation and the President of the Exchange". Based on the said view, it was ordered "in the interest of fostering investor confidence and for promoting transparency and the integrity in the functioning of the capital market, in exercise of powers under section 11 and 11B of the SEBI Act, 1992, read with Securities Contracts (Regulation) Act, 1956".

In Aggarwal's case also the Tribunal had examined the scope of section 11B in the light of various court decisions and upheld the "authority of the Respondent to issue directions of the type impugned". The Tribunal did not view the said direction as a penalty. I do not see any reason to take a different view on the Respondent's authority to issue a similar restraint order on Shri Rathi. A restraint order like this is not a penalty. Whether a direction is penal or not depends on the factual position. In Sterlite case, there was sufficient ground to view that the direction issued by SEBI was punitive. It is to be noted that the charges against Shri Aggarwal as extracted above was more serious and still the direction against him was confined only to the extent of making him ineligible to be a member of the Governing Board or office bearer of the exchange as well as any capital market related public institution for a period of 2 years.

In the case of J C Parekh, who was President of BSE, during the year 1998-99 the Respondent had passed an order under section 11 and 11B of the Act on March 23, 1999 directing Shri Parekh to relinquish the office of President of BSE and treating him ineligible to hold any public position as a member or the office bearer of the exchange as well as any capital market related public institution for a period of 3 years. The order was challenged before the then existing Appellate Authority. The gravity of the charge leveled against Shri Parekh could be seen from the following observations made by the Appellate Authority in its order.

> **"It is clear that the President, exceeding his powers directed that the Stock Exchange be opened beyond normal trading hours. During this time, only certain transactions were entered into. There was a complete lack of transparency in this issue. We are unable to appreciate why these developments regarding opening of Exchange beyond normal trading hours were not reported to the Board immediately. Not only that, vital information relating to the broking concern in which Vice President was associated was not given to the Board while other transactions were reported in the meeting of the Board of Governors on 14th June. Also earlier while the crisis was developing the margins were reduced, instead of being increased, in May, 1998 with result that large positions developed in certain scrips. Not only that, the margins were taken in the form of shares of companies, in which large positions had developed instead of shares of some other companies It was also noticed during the inquiry that a number of brokers were in fact attached to one client which could be traced to Harshad Mehta. The President directed these operations be done even subsequent to 14th June. No permission of the Board had been obtained for continuing this practice which was clearly in violation of the norms. It is, therefore, clear that the allegations which have been found proved against him are of serious nature. If Presidents of stock exchanges, particularly that of an important one in India namely the BSE, violates norms of exchange and disregards regulations then it is necessary that a deterrent action is taken to save the investors from possibility of any such future attempts and bring transparency"(Appellate authority order dated 9.4.1999 in J.C.Parekh's appeal before the Appellate Authority). The Appellate Authority upheld the Respondent's order referred to above. The Writ Petition filed by Shri Parekh in the Hon'ble Bombay High Court against the said order is pending.**

The charges leveled against Shri Parekh in the Respondent's order as confirmed by the Appellate authority are of far more serious nature having a direct bearing on the integrity of the market and interests of investors. But still, the direction was confined only to making him ineligible to hold any public position in future as a member of the Governing Board or the office bearer of the Exchange as well as any capital market related public institution. Exactly the same type of order was made in the case of R.K.Aggarwal also. The disqualification in

these cases was restricted to holding managerial positions in the exchange or any capital market related public institutions. The broking outfits owned or controlled by them were not suspended. But in Shri Rathi's case the restraint order has extended to holding any position as a director or a trustee of any capital market related entities also in addition to the capital market related institution (not only specific to capital market related public institutions). Further the registration to carry on broking business granted to two of his broking companies has also been cancelled.

The decision to direct Shri Rathi not to be in the management of stock market related institutions as a director or trustee is justified for the reason that by obtaining information from the Surveillance Department he had violated the norms of the three circulars governing the surveillance regime in the exchange. There is no other proven charge against him, though the show cause notice issued to him stated prima-facie violation of several Regulations. There is no finding that Shri Rathi or the companies controlled by him had misused the information so obtained by him. To put it the other way, the only charge that has been established against him is the original charge stated in the first order dated March 12, 2001 made, even before hearing him that "Anand Rathi as a Member and President of the Mumbai Stock Exchange has obtained information from Arun Dhanawade from the surveillance department. Such action is against the stated directions of SEBI and also leads to an absence of level playing fields amongst all brokers wherein some brokers have more information than the other brokers. Further such an action would also cause harm to the fairness, transparency and integrity of the stock exchange and the capital markets at large". In the order it was inter alia stated that "Shri Rathi is restrained from acting as a director member of the Governing Board of the stock exchange, Mumbai till further orders". The detailed investigation and enquiry conducted by the Respondent spanning over a period of 8 months have not established any other charge like violation of Insider Trading Regulations, UTP Regulations etc.

The Appellant in appeal No.53/2001 (Anand Rathi Securities Pvt. Ltd) by its own admission is a Broker, Merchant Banker and Portfolio Manager. The Appellant in appeal No.54/2001 (i.e. Anand Rathi Direct (India) Pvt. Ltd) is engaged in the business of sub broking.

On a perusal of the order it is found that the Respondent had accepted the Enquiry Officer's finding that there was no evidence against the Appellants to show that they had indulged in insider trading or market manipulations or that information obtained by Shri Rathi was used for the benefit of his companies. The Enquiry Officer recommended suspension of registration of both the Appellants companies under Stock Broker Regulations and Portfolio Manager's Regulations, though the Appellant in appeal No.54/2001 is not registered as a Portfolio Manager. In this context it is to be noted that even though the Appellant in appeal No.53/2001 is also a Merchant Banker, there is no reference in the show cause notice or in the inquiry report about this activity. It is also seen that though the Enquiry Officer had recommended suspension of registration of Stock Broker and Portfolio Manager of both the Appellant companies, there is no finding or decision on the Enquiry Officer's recommendation for suspending the registration as Portfolio Manager. In any case in the absence of any specific order, there is no bar on the Appellant companies on carrying on the said business. So the 'Merchant Banking' and 'Port Folio Manager' business remain unaffected by the impugned order, leaving the restraint order on Shri Rathi and suspension order of stock broking business on the Appellant companies.

It is seen from the impugned order that registration granted to do business as stock broker was suspended not for any omission or commission by the Appellant companies themselves but only because these companies are Rathi companies, ignoring that these companies are separate legal entities and that they have not used any information obtained by Shri Rathi from Shri Dhanawade on March 2, 2001. In this connection the reasoning putforth by the Respondent in its majority order need be looked into. Relevant para is extracted below:

> **Para 10.1: "It was further submitted that since Shri Rathi was elected President of the BSE by virtue of his being a director of a corporate broking entity, he could at the best personally be penalised. Another parallel argument was also advanced stating that the corporate entity should not be penalised for the delinquent acts of its individual directors.**
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> **We do not, in the facts of the case, find any merit in this submission. Admittedly, only one amongst the brokers, can become a President. Shri Rathi has broking entities and he is a director on the same. In the facts of the case, Shri Rathi is the guiding factor of the various associate entities. He is the man in control of management. Shri Rathi's**

entities owe their success and development to Shri Rathi. Further the contention that the entities (that is the companies) can not be held responsible for any acts of misdemeanor of its director is not acceptable in this case for another reason. The areas of activity of the entities and Shri Rathi's functions as the President of the Stock Exchange are the same i.e. activities related to the stock Market. These are so closely intertwined that it is difficult to draw a dividing line between the activities of the entities and Shri Rathi. We also find that in case if corporate broking entity, as is in the present case, it is one of the requirements that the whole time directors should have requisite qualifications and experience in dealing in securities. Further, they need to have atleast 40% share holding in such broking entities. This clearly reflects the heavy dependence of the entities on the directors. Therefore, in this case, the argument that the broking entities can not be held responsible for the action of Shri Rathi as President is difficult to accept. If his entity, Anand Rathi Securities Pvt. Ltd. had not been a broking entity, Shri Rathi could not have become the President of BSE. Shri Rathi undoubtedly acts on behalf of the companies. When the counsel for Shri Rathi was confronted with a query on the issue of whether the company could not be penalised for the acts of its directors even in the cases where there were findings of actual misuse of information by the broking entities, the counsel admitted that in such a case the broking entities could be penalised. We find that the Enquiry Officer has come to the conclusion that the information was obtained in relation to or for the benefit of his broking entities even though there was no occasion or necessity to use such information. As regards the earlier case involving former BSE President we find that the facts of the case were different. In that case, there was no instance of trading by his broking entities when the trading facility was opened after the trading hours. However, in this case there are some instances of trading by his associate entities but the Enquiry officer has given them the benefit of doubt as the preliminary investigation could not prove whether the said trading was done on the basis of information obtained by Shri Rathi.

Violation of Code of Conduct and Fit & Proper Criterion:

11.1: Shri Rathi & his associate entities contended that the act of seeking information by their director who was also the President of the Stock Exchange would not amount to any violation of Code of Conduct in respect of integrity and compliance of statutory requirements. It was stated that the integrity is to be judged in relation to the broking entities. As regards the requirement of "fit and proper", it was stated that the same is not applicable in the case of corporates or where no business is conducted and that the same is not a continuous requirement.

11.2 We do not find any merit in the above submissions. A stock broking entity and their directors/partners have to maintain the highest degree of integrity in all its activities or capacities. If a director or a partner of a broking entity is found involved for some serious offence, the same will also have a bearing on its broking activities. As regards the fulfillment of the fit & proper criterion if the submission of Mr.Rathi is accepted, it would mean a person who is "fit and proper" at the time of admission he need not be a fit and proper person when he actually conducts the business. Such a situation cannot be accepted in respect of broking business, which requires highest degree of integrity as the brokers who are entrusted with the monies or securities of the clients while conducting the business. This criterion has to be continually fulfilled otherwise we may end up in a paradoxical situation where a registered broker may not continue to fulfill eligibility conditions subsequent to the grant of registration. Even an entity after seeking registration, if it does not conduct business, this requirement is equally applicable as in the securities market the persons of doubtful integrity or a person who is not a "fit and proper" person are not considered eligible or fit for the purpose of engaging in the broking activities. This criterion is equally applicable in case of corporate sub-brokers also."

The argument that but for the nomination of Shri Rathi by the Appellant in appeal No. 53/2001, Shri Rathi could not have contested the election for membership in the Governing Board and that Shri Rathi being the nominee of his company the nominating company should be held liable for his conduct is very difficult to accept. I do not find any support to the Respondent's version from Rule 100A relied on by the Learned Advocate General. The reasoning provided in the order does not support the decision to suspend the registration. In this context the observation made by Shri D.R.Mehta, Chairman SEBI differing with the majority views is also worth referring to. He has stated:

"While I agree with my two learned colleagues in respect of their findings and order for Shri Anand Rathi, Navratan Securities and Rathi Global Finance ltd., I am not inclined to go along with them in the matters of Anand Rathi Securities P.Ltd and Anand Rathi Direct (I) Ltd.

The finding of the Investigating Officer, with whom the Enquiry Officer has also concurred with, is that there is no adequate evidence that the price sensitive information which Shri Anand Rathi, as the President of BSE got from the Surveillance Department of BSE, was either used by him or any of his broking entities / associates. Consequently the question to be addressed is whether his broking entities/associates namely Anand Rathi Securities Pvt.Ltd., and Anand Rathi Directo India Ltd, could be penalised, particularly when they had not used the information to their advantage. Put differently, can a company be vicariously liable for an act of its director acting in a different capacity?

During the arguments the counsels for the above mentioned companies contended that there was no provision in the Companies Act, 1956 which would hold the company responsible for the acts of its directors which were performed by them in their capacities other than those of directors and when their actions could not be ascribed to the company. In the subsequent written arguments also submitted by them, it was re-stressed that a company could not be penalized for the acts of its directors when the said acts had not been done either in the course of the employment or in the discharge of their duty as directors in their company. Legally, this argument carries conviction. Even though Shri Rathi could become the President of BSE by virtue of his directorship in his broking companies (this being the eligibility criterion for election as Director and subsequently as the President of BSE), his functions and actions as the President of BSE were separate and distinct from those of his broking entities /associates. It is true that for the wrongful actions of the company, the directors can get penalised. The reverse of this, however, may not be true unless there are some special circumstances such as the company taking advantage of the role of that director in his other capacity. Thus, in my view, the acts of Shri Rathi and the action against him in the present case, for which my two learned colleagues and I have concurred, cannot be judicially considered as a violation of requirement of being "Fit and Proper" or Code of Conduct so far as these corporate entities are concerned. We are also informed that Shri Rathi had ceased to be a director of these corporate bodies, which are under consideration.

The situation, however, would have been different if the broking entities of Shri Rathi had misused the information, which he obtained from the Surveillance Department. I am also not ruling out certain other special situations when the misdemeanours could impinge on the fitness or credibility of the company. In the circumstances of the present case I do not find any such nexus.

In view of the above discussion, the next issue to be dealt would be the way in which the period of restraint imposed on Navaratan Capital, Rathi Global, Rathi Direct India Pvt.Ltd and Anand Rathi Securities Pvt. Ltd, under section 11 and 11B of the SEBI Act, 1992 should be treated. The restraint orders under sections 11 and 11B of SEBI act were passed on 12th March 2001. These were issued because of the apprehensions of the possible misuse by his broking entities /associates of the information, which Shri Rathi got from the Surveillance Department of BSE. These orders were considered twice by the SEBI Board and confirmed as precautionary measures pending investigation /enquiry. Even the Hon'ble Bombay High Court did not interfere with the order but observed that SEBI should complete enquiry early and thereafter pass a final order. It was thus pro tem measure. However, the Investigating Officer did not find adequate evidence of misuse of the information by these entities / associates. The Enquiry Officer also agreed with the findings of the Investigating Officer and accepted explanation given by these entities. Thus, in the circumstances the restriction imposed on these broking entities / assocaites was justified. However, in the context of these findings and views, the restrictions cannot now stand.

In view of the above, as already stated, while agreeing with the direction /decision of my learned colleagues about Shri Anand Rathi personally and two of his entities namely Navaratan Capital & Securities Ltd, and Rathi Global Finance Ltd, I, in exercise of my quasi judicial powers, hold that the notices in respect of:

a. Anand Rathi Securities P Ltd.,

b. Anand Rathi Direct (I)Pvt.Ltd

are discharged and these entities are not cosidered liable for any penalty of suspension under Regulation 26 of SEBI (Stockbroker and Sub broker) Regulations, 1992."

It is to be noted that the Respondent has not put any restraint on Shri Rathi directly dealing in shares as a stockbroker or acting as Chief Executive of any broking entity, meaning thereby that he is free to do stock broking business. He is disqualified only from holding directorship or trusteeship of any capital market related entity, which can be even a private limited broking company. There is no bar on Shri Rathi setting up a large broking firm and managing the same. It is thus clear that Shri Rathi was not found to be unfit to carry on stock broking business and handle investors scrips /funds. If Shri Rathi is a fit and proper person to do business, following the same yardstick the entities owned and controlled by him also should be eligible to carry on business. Since the suspension of registration of the two Appellant companies is linked to the conduct of Shri Rathi, for the reason stated above, their suspension is not tenable. Further, I find force in the reasoning given by the Chairman in his differing order, as to the reach of action to the said two Appellant companies. For the reasons stated above the order suspending the registration of the Appellant companies is not tenable and deserves to be set aside. I do so.

In view of my finding that the Respondent's order against Shri Rathi made under section 11B is not a penalty and further that the penalty of suspension of registration awarded in the case of the two Appellant companies having been found unsustainable I do not consider it necessary to discuss the various authorities cited by the learned Counsel for the parties on the principles and circumstances governing imposition of penalties, etc.

In respect of the restraint order passed against Shri Rathi I am of the view that in the light of the nature of the direction issued by the Respondent in the case of Shri R. K. Aggarwal and Shri J. C. Parekh who were allegedly found interfering with Surveillance Department rather more intensely, the restraint order in the case of Shri Rathi also in all fairness be confined to "holding any public position as a member of the Governing Board or the office bearer of the exchange or any capital market related public institutions" and not to extend to holding directorship or trusteeship in any other entities. It is to be noted that the only charge finally held against Shri Rathi in the impugned order as against several serious charges like violation of Insider Trading Regulations, UTP Regulations etc. found in the show cause notice, is an act of impropriety of breaching the norms set out in the circulars issued by the Respondent governing the functioning of the Surveillance Department in the stock exchanges. The Respondent itself has after detailed investigation and enquiry concluded that the information obtained by Shri Rathi was not made use of by him or his companies for profit making and that his action has not actually resulted in benefitting him or his broking companies or caused any loss to anybody. Shri Rathi was subjected to investigation and enquiry in the context of the havoc witnessed in the market on March 2, 2001, to find out whether his action had in any way contributed to the same. Respondent after detailed enquiry has given him a clean chit absolving him of any role in depressing the market. It is therefore felt that restraining Shri Rathi holding directorship etc., for a period of two years is disproportionate to the gravity of the wrong doing by him and the actual fall out thereof. It is all the more so, in view of the fact that Shri Rathi is not barred from carrying on the business of stock broking in any manner, by the order. In fact the impugned order itself has impliedly restricted the disqualification that Shri Rathi is "not a fit and proper person" for a period of just nine months as could be viewed from the suspension order passed against his two companies, by limiting the period of suspension to nine months. Thus, taking into consideration the totality of the facts and circumstances of the case, it is felt that it would be but fair and reasonable to restrain Shri Rathi holding any post of director / office bearer of stock exchanges for one year. Accordingly that portion of the impugned order relating to Shri Rathi is modified as under.

"Shri Anand Rathi be restrained from holding any position as a member of the Governing Board or office bearer of any stock exchanges as well as any capital market related public institutions for a period of one year from March 12, 2001"

The order as modified to extent applicable to Shri Rathi is to be sustained. That part of the order suspending the registration granted to the two Appellant companies is set aside.

The appeals are disposed of in the above lines.

By way of postscript, I would like to state that it is high time that the stock exchanges are

liberated from the control of the brokers. Stock exchanges should no longer be allowed to be run as exclusive clubs of the brokers, by the brokers, for the brokers. Perhaps a totally broker-less management of the exchange would be the answer in this regard. I would suggest that the authorities may adopt appropriate measures to streamline the stock exchange management to impart more credibility to the institution to enhance the common investors' faith in the capital market.

(C.ACHUTHAN)
PRESIDING OFFICER

Place:Mumbai
Date: February 28, 2002