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W.P.No.13813 of 2023

IN THE HIGH COURT OF JUDICATURE AT MADRAS

RESERVED ON : 01.08.2024

PRONOUNCED ON : 14.10.2024

CORAM

THE HONOURABLE **DR. JUSTICE ANITA SUMANTH**

WP.No.13813 of 2023

Vimal Kumar Gupta

... Petitioner

Vs.

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

2.Securities Exchange Board of India,
Plot No.C4-A, G Block, BKC Bandra (East),
Mumbai – 400 051.

And also at
7th Floor, 756L, Anna Salai,
Chennai-600 002.

... Respondents

PRAYER: Writ Petition filed under Article 226 of the Constitution of India praying to issue a Writ of Declaration, to declare the Circular dated 02.09.2022 vide Ref No.NSE/INSP/53525 issued by the 1st Respondent to all Trading Members as illegal, arbitrary, non-est, perverse and contrary to law in as much it advises the Trading Members to refund the penalty levied on account of the



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“short/non-collection of upfront margins” to clients if the same has been passed on to the clients after 11th October, 2021.

For Petitioner : Mr.K.Jagannathan
For Respondents : Mr.P.Giridharan (R1)
Mr.C.Prasanna Venkatesh (R2)

ORDER

An interesting issue arises for decision in this matter. The petitioner is an investor, and a trader in shares and securities. He is a client of HDFC Securities Limited (in short ‘HDFC’), which is a trading member (in short ‘TM’)/stock broker with the National Stock Exchange of India (in short ‘NSE’/’R1’).

2. HDFC is not a party to this Writ Petition and there have been some submissions by respondents counsel urging that the Writ Petition is not maintainable for want of necessary/proper party. I will deal with this shortly.

3. The prayer in the Writ Petition is for a declaration to declare Circular dated 02.09.2002 issued by R1 as illegal, arbitrary, non-est, perverse and contrary to law inasmuch as it advises the trading member to refund the penalty levied on account of short/non-collection of upfront margin to clients, if the same has been passed on to the clients after 11.10.2021.

4. The first objection to the prayer is that Circular dated 02.09.2022 is a beneficial Circular and by seeking declaration of this nature, the petitioner has,



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in fact, sought removal of a benefit that has been granted by the respondents.

In arguing so, I believe that the respondents have lost sight of the fact that the challenge is qua the fixation of the date, 11.10.2021 and not to the Circular perse. What the petitioner is aggrieved by is the restriction under the Circular to refund the penalty levied on account of short/non-collection of upfront margin to clients, *if the same has been passed on to the clients after 11.10.2021*.

5. The benefit of the Circular has been made unavailable to those situations where the penalty has been passed on to clients prior to 11.10.2021. A distinction is thus made between those clients who have received demands of penalty before and after the stipulated date, that is, 11.12.2021 which is what the petitioner assails. I am of the view that the objection raised in this regard is myopic, does not have any merit and reject the same.

6. There is yet another objection on maintainability. The petitioner was aggrieved with the levy of penalty by the TM /HDFC and had also challenged the same before the GRC. An order has also been passed by the GRC on 31.03.2023. However the petitioner has neither challenged that order nor has he disclosed the litigation in that regard in the pleadings.

7. It is right that the Writ affidavit does not contain any discussion with regard to the proceedings before the GRC or the order passed by it. The writ



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affidavit proceeds as though the matter is a Public Interest Litigation. However, the explanation tendered is that the GRC was statutorily bound by the Circulars issued by the NSE and could not have adopted a stand contrary to the same. Hence, there would have been no purpose served in challenging that order. It is hence that the Circular has itself been challenged before this Court. I find merit in this submission.

8. Having said so, undoubtedly, there is a lacunae in the pleadings. The basis of the petitioner's challenge is the restriction in Circular dated 02.09.2022. The writ affidavit is however bereft of any facts in regard to the case that has been filed by the petitioner before the GRC culminating in order dated 31.03.2023. There are no particulars relating to the penalty imposed or how it has been treated by the GRC and to this extent the background is entirely lacking.

9. However, I would not put this aspect of the matter against the petitioner as there is nothing the petitioner would have gained in not disclosing the background to the matter in the writ affidavit. I believe that it is an omission but does not amount to suppression that would have been fatal to its cause.

10. It cannot be that the petitioner is not entitled to challenge the Circular itself. Such challenge would also not amount to a Public Interest Litigation as



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the restrictive covenant in the Circular has had a direct and detrimental effect on the petitioner's own case.

11. Hence, apart from the aspect of non-disclosure which I hold to be a lapse, albeit an innocuous one, I find that the Writ Petition is maintainable as it raises an important question for resolution. There are no disputed facts and the challenge can well be decided as a pure question of law, having regard to the width of power available to this Court under Article 226 of the Constitution of India. In light of this discussion, this Writ Petition is held to be maintainable.

12. The detailed submissions of Mr.K.Jagannathan, learned counsel for the petitioner, Mr.P.Giridharan, learned counsel for R1 and Mr.C.Prasanna Venkatesh, learned counsel for R2 have been heard.

13. The submissions of the petitioner are that Circulars issued by the SEBI in exercise of powers under Section 11(1) of the Securities and Exchange Board of India Act, 1992 read with Section 10 of the Securities Contracts (Regulation) Act, 1956 are for the protection of the interests of investors. A series of Circulars have been issued over the years, specifically providing for the levy of penalty on trading members for short collection/non-collection of margin from clients in Equity and Currency Derivative segments.



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14. Mr.Jagannathan would take me through the Circulars pointing out that the first of Circulars comes into effect on 01.09.2011. The second Circular is dated 07.09.2016, and stipulates that the penalty collected for short collection/non-collection of margins from clients should be credited to the Investor Protection Fund.

15. Vide Circular dated 01.08.2019 the imposition of fine for false/incorrect reporting of margin or non-reporting of margin by a trading member was rationalised. The contents of the aforesaid Circular were reiterated under Circular dated 12.10.2021 and then again under Circular dated 02.09.2022.

16. In the last of the Circulars, NSE has added a further stipulation that *'Further, Members are advised to refund the penalty levied by clearing corporations on account of "short/non-collection of upfront margins" to the clients on an immediate basis if same has been passed on to the clients after 11th October, 2021.*

17. The petitioner challenges the fixation of date as 11.10.2021. This is evidently for the reason that in his case, the penalty has been imposed and collected prior to 11.10.2021. The petitioner would argue that there is no



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rationale for the fixation of the said date, particularly seen in the context of the Regulation that is in effect from 2011 onwards. Thus, since trading houses were being cautioned from 2011 to desist from imposition of penalty for short levy/non-collection of upfront margins in specified conditions, all such situations should have been granted the benefit of Circular dated 02.09.2022 without any stipulation of date.

18. Per contra, Mr.Giridharan would argue that the Circulars issued by R1 constitute policy decisions and hence there is no avenue for the petitioner to seek any intervention in the same. These Circulars are issued after a deep analysis of market conditions and investment patterns and there is no justification for the petitioner to challenge the same.

19. Heard all learned counsel.

20.On 10.08.2011, SEBI issued a Circular relating to short collection/non-collection of client margins in Derivative segments. Para 1 of the Circular reads as follows:

Securities and Exchange Board of India
CIRCULAR

CIR/DNPD/7/2011
2011

August 10,

To
Managing Director/Chief Executive Officer
Recognized Stock Exchanges



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Dear Sir/Madam,

Sub: Short-collection/Non-collection of client margins
(Derivatives Segments)

1. In consultation with BSE, MCX-SX, NSE and USE, it has been decided that Stock Exchanges shall levy penalty specified hereunder on trading members for short-collection/non-collection of margins from clients in Equity and Currency Derivatives segments:

For each member	
'a'	Per day Penalty as % age of 'a'
(<Rs 1 lakh) And (<10% of applicable margin)	0.5
(≥ Rs 1 lakh) Or (≥ 10% of applicable margin)	1.0

Where a = Short-collection/non-collection of margins
per client per segment per day

.....

21. The Circular went on to stipulate different circumstances where there could be a short/non-collection of margins and set out various parameters that would be applicable in those different situations.

22. On 07.09.2016, a Circular was issued by SEBI setting out a mechanism for regular monitoring of, and imposition of penalty for short collection/non-collection of margins from clients. Paragraph 1 of Circular dated 10.08.2011 was reiterated therein and other stipulations also set out to address



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different situations of non/short levy. This Circular states that the penalty collected should be credited to the Investor Protection Fund.

23. On 01.08.2019, the rationalization measures continued, and it was stated that earlier Circulars dated 10.08.2011 and 07.09.2016 stood rescinded.

Clause 3 of this Circular stipulated as follows:

Securities and Exchange Board of India
CIRCULAR

CIR/HO/MIRSD/DOP/CIR/P/2019/88 August 01, 2019
To

The Managing Directors/Chief Executive Officers of
All Recognized Stock Exchanges
All Recognized Clearing Corporations

Dear Sir/Madam,

Sub: Rationalization of imposition of fines for false/incorrect reporting of margins or non-reporting of margins by Trading Member/Clearing Member in all segments.

.....

3. In order to rationalize and bring uniformity in the manner of imposition of fine for 'false/incorrect' reporting of margin vis-à-vis 'non-reporting' of margin, following guidelines are issued:

a. The Stock Exchanges and Clearing Corporations, in all segments, in consultation with one another, shall devise a standard framework for imposition of fine on the Trading Member/ Clearing Member for incorrect/false reporting and non-reporting of margin collected from the clients.



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b. Considering the principle of 'proportionality', the fine shall be charged to the member based on the materiality of non-compliance done by the member which may include factors such as number of instances, repeated violations, etc. The amount of fine to be charged upon the member may extend to 100% of such false/incorrectly/non reported amount of margin and/or suspension of trading for appropriate number of days.

24. Under clause 6, all Stock Exchanges and Clearing Corporations were directed as follows:

a. Bring the provisions of this circular to the notice of their members along with illustration as required and also disseminate the same on their websites.

b. Make necessary amendments to the relevant bye-laws, rules and regulations for the implementation of the above directions in co-ordination with one another to achieve uniformity in approach.

c. Communicate to SEBI, the status of the implementation of the provisions of this circular in their Monthly Development Reports.

25. On 12.10.2021, Circular Reference No.48/2021 was issued making reference to Circular dated 31.07.2020 and reiterating that members cannot pass on penalty with respect to short collection of upfront margins to clients.

Under Circular dated 31.07.2020, question and answer No.15 read as follows:



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15. In case of short reporting of margin/margin on consolidated crystallized obligation/MTM, can member pass on the penalty to the clients?

In case of failure (cheque not cleared or margin* requirement not met by the client) on part of the client resulting which penalty is levied by the Clearing Corporation on the member for short reporting of client upfront margins/margin on consolidated crystallized obligation/MTM losses, member may pass on the actual penalty to the client, provided he has evidences to demonstrate the failure on part of the client. Wherever penalty for short reporting of upfront margin/margin on consolidated crystallized-obligation/MTM losses is being passed on to the client relevant supporting documents for the same should be provided to the client.

*Member cannot pass on the penalty w.r.t.short collection of upfront margin to client.

26. This stood modified under Circular dated 12.10.2021 reading thus:

*'National Stock Exchange of India Limited
CIRCULAR*

<i>DEPARTMENT: INSPECTION</i>	
Download Ref No: NSE/INSP/49929	Date: October 12, 2021
Circular Ref. No:48/2021	

To All Members,

Sub: Guidelines/clarifications on Margin collection & reporting

.....

15. In case of short reporting of margin/margin on consolidated crystallized obligation/MTM, can member pass on the penalty to the clients?



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Member shall not pass on the penalty w.r.t. short collection of upfront margins to clients under any circumstances. In case of failure (requirement not met by the client) on part of the client resulting which penalty is levied by the Clearing Corporation on the member for short reporting of margins other than “upfront margins” such as consolidated crystallized obligation, Delivery margins, other margins (mark-to-market & additional margins), member may pass on the actual penalty to the client, provided he has evidence to demonstrate the failure on part of the client. Wherever penalty for short reporting of margins other than “upfront margins” is being passed on to the client relevant supporting documents for the same should be provided to the client.

.....'

27. The respondents would attempt to rely on the modification in the subsequent Circular. I do not agree. The opening part of the Circular makes it clear that the TM shall not pass on penalty with respect to the collection of upfront margins to clients under any circumstances. The rest of the answer relates to those circumstances where there have been a failure on the part of the client by virtue of it not meeting some requirements. If, and only if, as a consequence of such failure, penalty is levied, has the TM has been permitted to pass the actual penalty to the client provided that it has evidence to demonstrate and establish the clients's failure.

28. On 02.09.2022, NSE issues a Circular bearing Ref.No.60/2022 reiterating the earlier Circulars dated 31.07.2020 and 12.10.2021 and adding



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that if there was any levy of penalty for short/non-collection of upfront margin, it shall be refunded if the same had been passed on to the clients after 11.10.2021. The discrimination between two classes of investors, one who had been mulcted with penalty prior to 11.10.2021 and the other, after 11.10.2021, is what offends the petitioner.

29. All Circulars upto Circular dated 01.08.2019 have been issued by SEBI in exercise of powers conferred under Section 11(1) of the Securities and Exchange Board of India Act, 1992 read with Section 10 of the Securities Contracts (Regulation) Act, 1956 as a measure of protecting the interests of investors and securities and to promote the development and regulation of the securities market.

30. Subsequent Circulars dated 31.07.2020, 12.10.2021 and 02.09.2022 have been issued by the NSE only. Though NSE in its counter states that those Circulars were issued in consultation with SEBI, that statement is not supported by SEBI itself, and these Circulars appear to have been issued by SEBI unilaterally.

31. A specific query was put forth to Mr.Giridharan, learned counsel for SEBI as to whether any records were available to indicate discussion with SEBI prior to issuance of the three Circulars as aforesaid and he confirms that there



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are none. While the authority under which the Circulars have been issued is itself not in question, policy decisions that impinge on the rights of the investing public would have to be bound by Rules of proportionality and cannot be seen to be arbitrary or whimsical. That apart, it also does not seem appropriate that the NSE could impose a condition/restriction unilaterally in regard to a benefit that has extended by SEBI, without prior sanction/approval.

32. In the present case, it is the selection of the date, that is, 11.10.2021, that is the subject matter of challenge, and I am unable to find any support from the material on record as to the reason or basis for such selection. Apart from the offending date itself, there are other conditions that would have to be satisfied, for the refund of the penalty.

33. A perusal of GRC proceedings dated 31.03.2023 would reveal that the only reason why a portion of the relief sought for has been denied is the stipulation of the date as 11.10.2021 in Circular Ref.No.60/2022 dated 02.09.2022.

34. The circumstance set out under question and answer 15 in Circular No.48/2021 dated 12.10.2021 is thus, inapplicable to the present case. (see paragraph 27 supra). Such a conclusion emanates from a reading of the order of



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the GRC where the TM is not seen to have argued that there were failure/default on the part of the petitioners to justify passing on of the penalty.

35. Having considered the matter carefully, I am of the considered view that the selection/stipulation of the date as 11.10.2021 has no basis whatsoever. Such a stipulation had led to discrimination between two groups of investors, those who have been passed on the burden of penalty prior to 11.10.2021 and those who have suffered the burden post 11.10.2021. Thus, those investors who satisfy all the conditions under the Circulars but have suffered the passing on the penalty prior to 11.10.2021 have been left remediless.

36. The passing of the penalty for short-levy by the TM to the investor has been consistently decried by SEBI. In such circumstances imposition of a date after which only the penalty would be refunded has no justification whatsoever. This is contrary to Article 14 of the Constitution of India, affecting adversely one group out of two equally placed groups of investors.

37. That apart, the investor has no control over the date on which penalty is levied. Hence, there is serious prejudice caused by virtue of a fact that is outside the control of an investor, in respect of financial transactions that are identical to transactions by other investors, though of an anterior date.



38. In the present case, the satisfaction of the petitioner of the other conditions for refund constitute questions of fact and I extract below the findings of the GRC which are relevant and set the context for the grievance of the petitioner. To be noted that the GRC has passed the order after hearing both the petitioner and HDFC/TM.

Observations of GRC:

The Complainant has been trading with the TM from 2017 onwards and has been transacting all through financial year 2021-22. He has been a ultra-high net worth trader and is well versed with the market formalities. He claims that in the month of March 22 he was alerted by his auditor about margin penalty charges being debited in his account by the TM on a regular basis and he was shocked to see the huge debits in his account over the period of 1st April 21 to 8th March 22 amounting to Rs.8.83 Crs. He has claimed the reversal and refund of this amount by TM.

Considering the huge volume of business carried out by the complainant and the oral submissions made during the hearing, the complainant comes across as a seasoned trader and his claim that he has not seen the emails sent by the TM and is not aware that margin shortfalls attract penalties, seems to be a hollow claim and is not tenable. Having executed the RDD (Risk Disclosure Document) which forms part of the KYC, he is deemed to have fully understood the risks involved in the market and that payment of margins and penalty for non-payment of margins are integral to the F&O system of trading. It is the bounden duty of the client entering into the stock market to read, understand and assimilate the basic rules and regulations of trading in the F&O Segment in which he has been very active. He cannot turn a blind eye to the primary responsibilities cast upon



him to be vigilant of his trading account and to monitor and safeguard the credit in his trading account. Keeping quiet for almost a year (April 21 to March 22) when the margin penalties were regularly debited to his account and then to cry foul that he has been cheated by the TM does not augur well with the background and business stature of the complainant. To lament that the TM has not properly informed him about the imposition of penalty by NSE is a blatant lie as the TM has produced telephonic conversations had by their staff with the complainant, wherein the complainant acknowledges the shortfall of margins on his open positions and also agrees to take care of the penalties if any levied on the shortfall of margins.

On the part of the TM, he has got his share of mistakes, by allowing the complainant to continue his trading with the TM without collecting the margins fully on the trades. To presume and put out an argument that collection of upfront margin alone with absolve the TM of his responsibilities towards the trades of the client is a figment of his own imagination. Such a thesis on maintaining upfront margin alone is self-serving the TM to enlarge his business and cannot be accepted by this forum and is a violation of SEBI and NSE Circulars.

A strong urge to drive the business, by collecting the Upfront Margin alone & without taking the required steps to intervene at appropriate times and square off the open positions has turned out to be a preposterous idea for the TM. He has failed to realize that the penalty for margin shortages is basically levied on the Trading Members to ensure that they collect the margins fully from their clients and do not manipulate the margin system to benefit their business interest.

Because of this slip shot manner of doing business, the TM is now facing the situation of refunding a major chunk of margin penalties levied between 1st April 21 to 8th March 22.



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By their own submissions the TM has relied on two Circulars namely

- i. NSE/INSP/49929 dt 12th Oct 2021
- ii. NSE/INSP/53525 dt 02nd Sept 2022

From which it is very clear

a. that trading members are not permitted to pass on the penalty levied by clearing corporations on account of “short/non-collection of upfront margins” to clients under any circumstances

b. that members are advised to refund the penalty levied by clearing corporations on account of “short/non-collection of upfront margins” to the clients on an immediate basis if same has been passed on to the clients after 11th October, 2021.

By their own submissions the TM has quoted the above circulars in their replies and has also mentioned in his reply dated 4th March 23 that penalty on upfront margin cannot be passed to the Client from October 12, 2021.

Further vide their communication dated 29th March 2023, TM has given the break-up of the Rs.8.85 Crs as below:-

*period 1 - (1st April 21 to 11th Oct 21) – 5.08 Crs
and*

period 2 (12th Oct 21 to 8th Mar 22) – 3.77 Crs

The TM has also computed the penalty amount on account of non-payment of Mark to Market Margins from 12th Oct 21 to 8th Mar 22 as Rs 87,39,571.96/- which can be passed on to the client. This brings the net margin refundable for the period 12th Oct 21 to 8th Mar 22 to Rs 2.89 Crs.

Orders given by GRC:



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Both the parties were heard and explained in detail of their respective positions. Based on the above observations and documents perused, this panel is of the unified view that the TM being one of the premier broking institutions of the country has to strictly adhere to the circulars issued by the exchange. Hence they have to refund a sum of Rs 2.89 Crs with immediate effect following Circular No NSE/INSP/53525 dt 02nd Sept 2022.

39. The GRC has made it clear that the petitioner is, in fact, entitled to the refund and has ordered refund to the extent to which the Circular does not stand in the way. The decision adverse to the petitioner relates to that part of the penalty on upfront margin relatable to the period prior to 11.10.2021 only.

40. In light of the discussion as aforesaid, the stipulation relating to the date under Circular Ref.No.60/2022 dated 02.09.2022, is found to be arbitrary and is quashed. As a consequence, the prayer of the petitioner stands moulded to a challenge encompassing order passed by the GRC dated 31.03.2023 and such challenge is allowed and order dated 31.03.2023 set aside. The petitioner's application before the GRC restored to its file. The GRC shall issue notice to both the Petitioner as well as the TM/HDFC, hear them and decide the matter de novo. In doing so, the GRC shall not be circumscribed by the reference to the date '11.10.2021', in Circular No.60/22 dated 02.09.2022.



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41. This Writ Petition is allowed in the aforesaid terms. No costs.

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Index : Yes
Speaking Order
Neutral citation :Yes
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To

- 1.The National Stock Exchange of India,
Exchange Plaza, C-1, Block G,
Bandra Kurla Complex, Bandra (E),
Mumbai – 400 051.
 - 2.Securities Exchange Board of India,
Plot No.C4-A, G Block, BKC Bandra (East),
Mumbai – 400 051.
- And also at
7th Floor, 756L, Anna Salai,
Chennai-600 002.



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DR.ANITA SUMANTH,J.

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