

**BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI**

Appeal No. 98 of 2007

Date of decision: 6.6.2008

1. Vyomit Shares Stock & Investment Pvt. Ltd.
 2. Haresh Kantilal Dalal
- Appellants

Versus

1. Securities and Exchange Board of India
 2. Bombay Stock Exchange Ltd.
- Respondents

Mr. S.H. Doctor Senior Advocate with Mr. K. Setalvad and Mr. T. Mavani Advocates for Appellants.

Dr. Poornima Advani Advocate with Ms. Sejal Shah Advocate for Respondent No.1.

None for Respondent No.2.

Coram: Justice N.K. Sodhi, Presiding Officer
Arun Bhargava, Member
Utpal Bhattacharya, Member

Per: Utpal Bhattacharya, Member

In this appeal, the appellants have challenged the decision of the Securities and Exchange Board of India (the Board for short) to deny appellant no.1 the benefit of fee continuity in terms of paragraph I(4) of schedule III to the Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Regulations, 1992 (Brokers Regulations for short). The facts of the case in brief are that Shri Haresh Kantilal Dalal (Haresh), appellant no.2 herein, was an individual member of the Bombay Stock Exchange (BSE), registered with the Board since November, 1992. He, together with Shri Paresh Dalal (brother) and Shri Kamlesh Dalal (cousin), formed a company in the name and style of Vyomit Shares Stock and Investment Pvt. Ltd. (appellant no.1 herein) on May 4, 1995. At that time Haresh, Paresh and Kamlesh were the Directors of the company and each had 10 shares of face value Rs.100 each. On April 17, 1996, Haresh resigned as Director of the appellant company. On April 27, 1996 the shares of the company were subdivided into shares of face value Rs.10 each and the equity holding

of Haresh, Paresh and Kamlesh became 100 shares each. On June 14, 1996 Haresh's wife, Sonal Haresh Dalal, was allotted 180,000 equity shares and Rupesh Lakdawala, Haresh's brother-in-law, was allotted 120,000 equity shares of the appellant company. On June 25, 1996 the appellant applied for corporate membership of BSE. At that stage the Directors of the appellant company were Kamlesh Dalal, Kirti Shah and Rupesh Lakdawala.

2. On January 21, 1997 appellant no.1 was elected a corporate member of BSE. The individual membership card of Haresh was transferred to appellant no.1 for this purpose. On April 11, 1997 the Board granted a certificate of registration in favour of appellant no.1. The shareholding pattern of appellant no.1 both at the time of its election as a corporate member of BSE as well as at the time of registration by the Board was as follows:

| | |
|--------------------|----------------|
| Haresh Dalal | 100 shares |
| Paresh Dalal | 100 shares |
| Kirti Shah | 2,500 shares |
| Kamlesh Dalal | 2,600 shares |
| Rupesh Lakdawala | 120,000 shares |
| Sonal Haresh Dalal | 180,000 shares |

Appellant no.1 commenced trading on BSE with effect from May 12, 1997. On this date Haresh was allotted 100,000 redeemable non-cumulative non-participating 9% preference shares of face value Rs.100 each. In August 2004, the Board, sent to appellant no.1 a statement raising a demand of registration fee amounting to Rs.4,30,73,905 for the period up to 2001-02. Since the Board did not allow the fee continuity benefit, the appellants challenged the demand before this Tribunal in appeal no. 236 of 2004 which was remanded back to the Board with this Tribunal's order dated May 3, 2005 with a direction to pass fresh orders in accordance with law after granting the appellants an opportunity of hearing. The Board's order dated February 26, 2007 passed in pursuance of this Tribunal's direction reiterates its earlier decision to deny the fee continuity benefit to the appellant and has been challenged in this appeal.

3. The learned senior counsel for the appellants has argued that appellant no.1 is clearly eligible for the fee continuity benefit in terms of schedule III to the Brokers Regulations read with the Board's circular of February 6, 2004. This circular stipulates that brokers corporatised by conversion of individual/partnership membership cards prior to January 21, 1998 (and after 31st March, 1997) are eligible for fee continuity benefit if the conditions stipulated in the said paragraph are satisfied in spirit. It further elaborates the meaning of the expression "satisfied in spirit" in the following words:

"... It has been decided that the fee continuity benefit would also be available to the corporatisation done between April 01, 1997 and January 21, 1998 provided the converted corporate entity satisfies the conditions in spirit. For this purpose, the Exchange and broker concerned would be required to prove in each such case that the erstwhile proprietor/partner(s) continued to hold controlling stake or interest in the corporate member so converted for three years from the date of conversion...."

Such control, according to the learned senior counsel, can be direct through the personal shareholding of the individual or indirect, through the shareholding of relations or other close associates. It is the case of the appellants that appellant no.2 always held, directly or indirectly, the controlling stake in appellant no.1 thereby making the latter eligible for the fee continuity benefit as the converted corporate entity.

4. The learned counsel for the Board has advanced several arguments while contesting the claim of the appellants. Her first argument is that "satisfied in spirit" only means that all the conditions mentioned in paragraph I(4) of schedule III to the Brokers Regulations have to be satisfied, albeit not in strict terms. In her view, not only has the erstwhile member to have controlling stake or interest, the stake or interest has to be personally his and his alone. Indirect stake does not qualify in terms of the circular, according to the learned counsel, because paragraph 4 *ibid* does not leave any scope for any shareholding of any individual other than the erstwhile individual member to qualify for fee continuity benefit. The learned counsel for the Board has also argued that appellant no.2 did not resort to corporatisation of his proprietary firm for any business reason. It was only because in April, 1995 he was served with a charge sheet by the CBI

and he apprehended that he might shortly be disqualified from holding individual membership of BSE that he corporatised his business as a safeguard against that contingency. The counsel urged that corporatisation for such a purpose should not qualify for fee continuity benefit.

5. We do not find any merit in either of the arguments of the learned counsel for the respondent. In view of the clear and unambiguous stipulation in the Board's circular of 6.2.2004, there is no scope for arguing that "satisfied in spirit" means anything other than having controlling stake or interest for a period of three years from the date of conversion. Since the circular does not exclude indirect stake from being counted as part of the controlling stake, there is no case for holding that the controlling stake can only be direct stake. As regards the second argument of the learned counsel for the Board, we are of the view that the reason behind corporatisation is irrelevant for the purpose of fee continuity benefit so long as the conditions stipulated in the Brokers Regulations and other relevant circulars and orders of the Board are satisfied.

6. Having noted the arguments of the two opposing counsel, let us now examine whether in the specific facts and circumstances of this particular case the benefit of fee continuity should be extended to appellant no.1, considering the stake of the erstwhile individual member (Haresh), both direct and indirect, in the company. As we have already seen, at the time of incorporation, appellant no.1 had only three shareholders namely Haresh, his brother Paresh and his cousin Kamlesh, each of them holding 10 shares of Rs.100 each. At the time when appellant no.1 became a corporate member of BSE and also at the time when it was given registration by the Board as a broker, Haresh still had 100 shares of Rs.10 each but his wife Sonal Haresh Dalal had 180,000 shares which constituted more than 50 per cent of the issued equity capital of appellant no.1. Besides that, Rupesh Lakdawala, another close relation of Haresh had as many as 120,000 shares. Thus, it could be argued that till that stage, Haresh continued to have a controlling interest in appellant no.1 through his wife and other close relations. However, significant changes in the shareholding pattern of the company took place subsequently as under:

| | |
|-------------------|--|
| 22 October, 1997 | Transfer of 120,000 equity shares by Rupesh Lakdawala to Sonal Haresh Dalal. |
| 20 March, 1999 | Transfer of 100 equity shares by Haresh to Sonal Haresh Dalal, leaving no equity with Haresh. |
| 28 November, 2000 | 100,000 preference shares of Haresh redeemed by appellant no.1. |
| 6 October, 2001 | Transfer of 144,500 equity shares by Sonal Haresh Dalal to Haresh. |

As is clear from the foregoing table, on 20.3.1999 Haresh divested himself of all equity shares in appellant no.1 though on 6.10.2001, he again acquired substantial quantity of shares from his wife Sonal. In between, on 28.11.2000 Haresh got his preference shares also redeemed by appellant no.1, thereby extinguishing even his remaining financial interest in the company. Thus, between 20.3.1999 and 6.10.2001, Haresh had absolutely no equity shareholding in appellant no.1. In order to consider if Haresh had a controlling stake or interest in appellant no.1 for the purpose of fee continuity benefit, we have to be clear about what the meaning of the expression “controlling interest” is. Black’s Law Dictionary defines “controlling interest” as “sufficient ownership of stock in a company to control policy and management.” This can be elaborated as meaning that controlling interest is the power of controlling by votes the decisions of the company in the shape of resolutions passed at general meetings. Clearly, a person who is not entitled to attend any general meeting of a company because he is not a member of the company cannot be acknowledged as one who controls the voting in the general meeting. Such control in absentia cannot be accepted. Therefore, the argument of appellant no.1 that so long as Haresh’s wife and other close relations had majority shareholding in the company, Haresh could be taken to have a controlling stake in it cannot be accepted as valid when he has absolutely no equity shares in the company and ceases to be a member thereof. Otherwise even a complete outsider having no connection with a company can be presumed as having a controlling stake therein if his close relations and associates control such a company. Apart from being utterly

illogical, such a view cannot but lead to chaos. Unless this threshold of membership of the company is crossed, there is no scope of considering whether such a person has indirect stake in or control over the company through shareholdings of his relations and associates. In the present case Haresh ceased to be a member of appellant no.1 on 20.3.1999 which means that he had remained a member of the company for only 2 years and 2 months since 21.1.1997 when appellant no.1 was converted as a corporate member of BSE. This period falls short of the period of three years prescribed in the Board's circular of 6.2.2004 ibid and therefore appellant no.1 cannot be considered to be entitled to the fee continuity benefit in terms of schedule III to the Brokers Regulations.

In view of the reasons stated above, we dismiss the appeal with no order as to costs.

Sd/-
Justice N. K. Sodhi
Presiding Officer

Sd/-
Arun Bhargava
Member

Sd/-
Utpal Bhattacharya
Member

6.6.2008
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