

## Order

### In the matter of First Global Stock Broking Pvt. Ltd. & Vrudhi Confinvest (I) Pvt. Ltd.

#### **1.0 Background**

1. **Securities and Exchange Board of India (hereinafter referred to as "SEBI") undertook investigations on observing that there was excessive volatility in the index movements of stock exchanges during mid February to early March 2001 and that there were apprehensions of attempts by certain entities to distort the true price discovery and manipulate the securities markets.**
2. **Preliminary investigations were carried out by SEBI to find out the role of various entities including entities controlled and connected by/ with Mr. Shankar Sharma and Mrs. Devina Mehra, like First Global Stock Broking Pvt. Ltd., (hereinafter referred to as "FGSB"), a SEBI registered stock broker, Vrudhi Confinvest India Pvt. Ltd. (hereinafter referred to as "VCIP") Sub broker. The said investigations prima facie revealed that the FGSB and VCIP indulged in large trading transactions in the scrips of Global Telesystems, HFCL, DSQ Software, Zee Telefilms, Wipro, Satyam Computers, MTNL, SBI, Infosys Technologies and Sterlite Optical. It further appeared that these large trading transactions including short sales transactions were carried out to artificially depress the prices of the above named securities.**
3. **The pattern, inter alia, of large carry forward sales, sales in certain scrips on specific dates, order placement particularly in the time slots when the scrips prices registered substantial fall, portfolio operations disguised as structured arrangements in the garb of arbitrage trades, routing of proprietary trades through non-descript unregistered sub-broker to hide the proprietary trades all prima facie indicated a concerted attempt to artificially depress the prices of above said scrips and to hide the proprietary trades and portfolio operations.**
4. **All the above activities appeared to have been carried out in a manner which is detrimental to the interest of investors as well as safety and integrity of the securities market and which would lead to interference with the fair and smooth functioning of the market. The conduct of FGSB and VCIP did not appear to be in consonance with the high standards of integrity, fairness and professionalism expected from a Stock Broker and Portfolio Manager.**
5. **After taking into consideration the available material, SEBI passed an interim order dated 18<sup>th</sup> April 2001 debarring Shankar Sharma, Devina Mehra, FGSB and VCIP (hereinafter called as FGSB & Associates) from undertaking any fresh business as Stock Brokers or Merchant Banker or Portfolio Manager till further orders are passed by SEBI in this regard. It was also ordered that a post decisional hearing be given on 30<sup>th</sup> April, 2001.**
6. **FGSB and associates did not avail the opportunity on 30<sup>th</sup> April, 2001 but filed a Writ Petition (L) no 1129/2001 before Hon'ble High Court of Mumbai. During the hearing before Hon'ble High Court on 4<sup>th</sup> May 2001, FGSB and associates stated before the Hon'ble High Court that in order to establish their bona fides and without prejudice to their rights and contentions, they would not undertake fresh business as stockbrokers or merchant bankers or Portfolio Managers till further orders are passed by SEBI. In view of the said undertaking the Hon'ble Court was pleased to dispose of the petition by directing the petitioner to file their reply and appear before SEBI on a date fixed by SEBI within the prescribed time limit set by the Hon'ble High Court and further, inter alia, directed that in view of the statement made by FGSB and others the directions contained in the impugned order dated 18<sup>th</sup> April 2001 do not survive and the said Order and the affidavit filed by SEBI in the said writ petition will be treated as a show cause notice to the petitioners.**
7. **Accordingly, FGSB filed their written reply to SEBI on 11<sup>th</sup> May 2001 after inspecting the documents relied upon by SEBI for passing the order dated 18<sup>th</sup> April 2001. An opportunity of personal hearing was given on 18<sup>th</sup> May 2001 and FGSB and Associates availed the opportunity.**
8. **After considering the said written replies and oral submissions, SEBI passed a reasoned Order on 25<sup>th</sup> May, 2001. By the said Order dated 25<sup>th</sup> May, 2001 FGSB and Associates were restrained from undertaking any fresh business as Stock Broker, Merchant Banker and Portfolio Manager pending enquiry. An enquiry officer was appointed vide a separate order dated 31<sup>st</sup> May, 2001 to enquire into allegation of violation, inter alia, SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995. SEBI (Stock Brokers and Sub Brokers) Regulations, 1992 and SEBI (Portfolio Managers) Regulations, 1993.**
9. **FGSB and Associates, being aggrieved by the said Order dated 25<sup>th</sup> June 2001 filed an Appeal before the Securities Appellate Tribunal. The Tribunal, on an interim application made by FGSB & Associates, passed an Order dated 25<sup>th</sup> June, 2001, declining to grant interim relief for the reasons stated therein. The aforesaid Appeal shortly thereafter came up for hearing and final disposal, when the Tribunal after hearing the parties passed a final order dated 19<sup>th</sup> September, 2001. By the said order the Hon'ble Tribunal, inter alia directed SEBI to complete the inquiry within 10 weeks from the date of the said order dated 19<sup>th</sup> September, 2001 failing which the order dated 25<sup>th</sup> May, 2001 would cease to operate.**

The Hon'ble Tribunal was pleased to hold in the said order that SEBI had powers to pass order dated 25<sup>th</sup> May 2001 and on the issue of alleged malafides held as under:

"The Appellants' contention that the order has been made malafide and for extraneous reasons, remains unsubstantiated. I do not find any force in linking inquiry with "tehelka expose" as alleged. By the Appellants' own version the enquiry started on 2<sup>nd</sup> March 2001 with NSE/BSE asking for various information relating to the transactions. It was a preliminary data collection exercise at that point of time. The respondent entered the scene only subsequently on examining those materials and realizing the need to pursue the matter further. In the meantime "tehelka expose" happened. The enquiry was already on even before the tehelka expose. Therefore, it is not correct to link the enquiry with the tehelka expose. The Respondent's alleged request to provide details of the shareholding pattern of Buffalo Networks P Ltd. the owner of Tehelka.com, its financial statements, etc. does not establish any nexus between the inquiry and the expose. The appellants had admitted that they held 14.5% stake in the said Buffalo Network and in that context there is nothing unusual, if in an inquiry the details of the ownership, management and financial position of the invest company are sought. Further, no reason or any motive on the part of the respondent to act in any vindictive manner against the appellants has been even suggested. The respondent, which is an independent statutory authority is not a person directly or indirectly mentioned in the expose. Further it is also to be noted that the appellants are not the only person subjected to investigations by the respondent. Activities of several market intermediaries, not in any way connected with tehelka.com were also taken up for investigation. In the absence of sufficient material before me substantiating that the impugned order is malafide, the appellants' allegation fails."

The order further directed that all the contentions of the parties are expressly kept open. Respondent shall decide the matter without being influenced in any manner by the observations made in this order.

10. On 20<sup>th</sup> November, 2001 SEBI made an Application to the Tribunal for the reasons stated therein praying for extension of time for at least 12 weeks for the purpose of completing the enquiry proceedings and thereafter passing final order and praying therein that till then the Order dated 25<sup>th</sup> May, 2001 may remain operative.
11. The aforesaid Application dated 20<sup>th</sup> November, 2001 came up for hearing before the Tribunal on 28<sup>th</sup> November, 2001. After hearing, the Tribunal was by its Order dated 28<sup>th</sup> November, 2001 pleased to extend time for 5 weeks from the date of the order i.e. upto 2<sup>nd</sup> Jan 2002 to pass the final order.
12. SEBI filed another application on 28.12.2001 for further extension since the enquiry could not be completed. The Tribunal heard the parties on 1<sup>st</sup> January 2002 and vide its orders dated 2<sup>nd</sup> January 2002 extended the time for a further period of 5 weeks for completion of enquiry and to pass final orders. As per this schedule, the orders were to be passed on or before 6<sup>th</sup> February 2002.
13. FGSB and others filed Appeal No.2/2002 against SAT order dated 19<sup>th</sup> September 2001 before the Hon'ble High Court of Mumbai under Section 15Z of SEBI Act, 1992. The said appeal came up for hearing on 2<sup>nd</sup> April 2002 before Justice A P Shah and Justice V K Tahilramani. The Hon'ble High Court was pleased to dismiss the said appeal stating as under:

"The impugned order is only an interlocutory order pending enquiry by SEBI under Section 11 of the Act. The enquiry is complete and report is also submitted. However, final action has not been taken in view of the challenge raised by the appellant in Writ Petition (Lodging) no.304 / 2002. The submission of the learned Counsel for the appellant that SEBI has no power to pass such order cannot be accepted in view of the decision in Anand Rath v/s Securities and Exchange Board of India, 2001 SEBI & Corporate Laws Reports 227. Appeal is dismissed".

## **2.0 Show Cause Notice by Enquiry Officer**

1. The Enquiry officer issued show cause notice dated 17<sup>th</sup> July 2001 to FGSB and Associates containing the following charges :-
  - 2.2. that the entities had indulged in large trading transaction in the scrips of (1) Global Telesystems ,(2 ) HFCL,(3) Zee Telefilms ( 4 ) Wipro ( 5 ) Satyam Computers ( 6 ) MTNL ( 7 ) State Bank of India ( 8 ) Infosys Technologies ( 9 ) DSQ Software and ( 10) Sterlite Optical with a view to artificially depress the prices in the said securities between mid February and mid March 2001 in a concerted manner ; (2) that substantial net sales were carried over a period of time, on specific dates and in specific time slots ; (3) that the orders were placed in specific time slots when the scrip prices registered substantial fall; (4) that Portfolio operations disguised as structured arrangement were carried out showing them as arbitrage trades; (5) that proprietary trades were routed through non - descript unregistered sub broker to avoid detection; (6) that the conduct of Mr. Shankar Sharma and Mrs. Devina Mehra , Directors of FGSB were unbecoming of a stock broker and they did not exhibit high standards of integrity, fairness and professionalism of registered intermediary.

## **2.3 The imputation of charges in support of the aforesaid allegations are as under:-**

2.4 That the FGSB had undertaken substantial short-selling and unwinding of previously built long positions in the aforesaid 10 scrips with a view to artificially depress the share prices thereby resulting in the market movements adversely between mid-February and mid March 2001.

- a. Net sales by FGSB were about 14% in Wipro and 10% in HFCL, in Settlement No.48 at BSE.
- b. 14.5% of net sale in Wipro on the exchange on 1<sup>st</sup> March, 2001 to net sales of FGSB were 14.5% net sale of the exchange.
- c. On 2<sup>nd</sup> March, 2001, 10% of net sales in DSQ Software in NSE.
- d. On 23<sup>rd</sup> February, 2001, instances of significant net sales by FGSB during specific time slots constituted almost 45% of net sales in WIPRO at BSE between 10:40 – 10:58.

## 2.5 **Short sales :**

FGSB has indulged in short sales thereby causing a heavy fall in the prices of securities in the market. Details are as under:

- a. FGSB had a peak carry forward short sale of 50,000 shares of Wipro from Settlement no.47 to 50, having a value of around Rs.13 crores. The short sales were subsequently squared up in Settlement No.51 ;
- b. FGSB had a peak Carry forward short sale position of approx. 55,000 shares in the scrip of SSI between Settlement No.47 – 49 with an approx. value of Rs.6 crores. These sales were subsequently squared up in Settlement No.50 ;
- c. FGSB had Carry forward short sales from Settlement no.46 – 48, in Sterlite Optical with a peak position of 27,489 shares having value of around Rs.2 crores ;
- d. The substantial unwinding of long positions, short sale positions and sales deferral by the member in select scrips which were either part of stock indices or of significant momentum scrips, indicate a concerted attempt to hammer their prices and impact the market as a whole.
- e. Significantly, even the aggregate trading done by FGSB at BSE & NSE showed net sales of Rs. 28.82 crores on 13<sup>th</sup> February, 2001, Rs. 13.60 crores on 16.2.01, Rs. 21.46 crores on 19<sup>th</sup> February 2001, Rs. 20.92 crores on 23<sup>rd</sup> February ,2001, Rs. 2.18 crores on 1<sup>st</sup> March 2001 and Rs. 21.76 crores on 7<sup>th</sup> March .2001. The trading by the member in the aforesaid manner had followed a consistent bearish pattern and contributed in a major way to the fall in the market indices.
- f. FGSB had put sell orders and subsequently cancelled the sell orders in a concerted attempt to manipulate the share prices.

## 6. **Circular trading and routing of proprietary trades through unregistered entities:**

FGSB had conducted circular trading in order to manipulate the share prices and routed the proprietary trades through non-descript unregistered entities with a view to escape scrutiny. These transactions involving circular trading and routing of proprietary trades through third parties were not regular and transparent but had been entered with a view to manipulate the share prices and avoid detection.

Shri Shankar Sharma had indulged in circular trading by taking opposite positions at FGSB (in the name of Vruddhi) and Bang Equity by synchronizing the order timings for specific scrips, specific quantity and at specific rate. Trading had also been executed on dates when the member had adequate exposure limits available. The approximate value of such trades during the two settlements between February 20 and March 2, 2001 was upto Rs.50 crores.

The trading pattern of Shri. Shankar Sharma through Nirmal Bang and others were highly irregular and resulted in building up of concentrated positions to avoid detection. It is alleged that the circular trading between FGSB and Nirmal Bang Group for the proprietary trades of Shri. Shankar Sharma, have been structured by synchronizing the order entry in the system with a view to manipulate the market.

7. FGSB had conducted portfolio operations without complying with the SEBI (Portfolio Managers) Regulations, 1993 by ensuring a minimum rate of return to the clients and the transactions in the accounts were structured in the garb of arbitrage trades. The arrangement between FGSB and RNA Group tantamount to ensuring a definite return on investment and is highly irregular in nature and was not consistent with the regulations of stock broking.
8. Further, FGSB had traded through Nirmal Bang even on dates when FGSB had adequate exposure limits available on the exchange.

## 3.0 **Further Show Cause Notice :**

The Enquiry Officer issued a further show cause notice on 6<sup>th</sup> October 2001 containing following charges:

1. That FGSB has indulged in short sales which are not in compliance with SEBI Circular dated 7<sup>th</sup> March, 2001.

2. That FGSB had shown some of their proprietary trades executed by them as institutional trades though they were not institutional trades and thus evaded payment of margin money in respect of these transactions and by excluding these trades while calculating gross exposure and intra-day trading limits, the member had over- stretched trading limits.
3. That FGSB had not cooperated in the ongoing investigations into the irregularities regarding stock market volatility and even summons issued for furnishing of information were not complied with.

#### **4.0 Findings of Enquiry Officer**

1. FGSB and VCIP submitted reply to the said show cause notices. They were also given full opportunity of hearings on various dates. Various documents as requested by FGSB were furnished by the enquiry officer to FGSB and VCIP. They also submitted written submissions during enquiry proceedings. The Enquiry Officer after considering the replies, submissions and documents completed the enquiry as per the Regulations and submitted his report to the Board on 9<sup>th</sup> January 2002. The findings of the Enquiry Officer, in brief, are as under : -
2. In regard to "net sales at the exchange", FGSB had contented that it was not a correct parameter to compare with. The enquiry officer has given a view that the net sales of the member can be compared with the net sales at the exchange. It cannot be compared with the aggregate trading volumes, which comprises of both sales and purchases and such comparison would give a distorted view.
3. With regard to trading by FGSB at BSE, Enquiry officer has given the following findings-
  1. In the scrip of Global Tele Systems Ltd., the Enquiry Officer observed that the member had net sale of 89350 shares in settlement no 1050. The Teji badla position was reduced from 63810 shares to 16125 shares in this settlement. (settlement no.49 to settlement no. 50) which means there was further sales by the member.
  2. In the scrip of HFCL, the Enquiry Officer observed that the member had a net sale to the extent of 99166 shares in Settlement no. 1048, which constitutes 9.47% to the exchange net. 84000 shares delivery position of Vruddhi in the scrip was also taken note of.
  3. In the scrip of Satyam, purchase and sale position of the member prior to mid February had not been taken into account since the charge relates to artificially depressing the prices in the scrip between mid February to mid March. The carry forward sales of 85000 shares in Settlement No.1048 relate to proprietary trades done by Vruddhi.
  4. In the scrip of SSI, FGSB had contented that this is not one of the 10 scrips which was being enquired into. In this regard Enquiry Officer had given his finding that it is not correct to say that this is not one of the scrip being enquired into. There is a specific allegation of short sale in certain scrips including SSI. The member is under erroneous impression that only those trading transactions mentioned at page one in the show cause notice (dated 17<sup>th</sup> July 2001) should be enquired into and the rest are outside the purview of the show cause notice. Under the head of short sales, the allegations of short sales made by the member with a view to depress prices of securities is leveled and the details of such scrips were given in the Show Cause Notices. Therefore, the contention of the member is not tenable. It was also observed that there was a net sale of 10136 shares (which constituted 3% to the exchange). In Settlement No.1046 and 39479 shares (which constituted 9.10% to exchange net) in Settlement no. 1047. The total carry forward sales at the end of settlement No. 1047 were 50000 shares. In Settlement no. 1048, the total carry forward sales was 49000 shares and in Settlement no. 1049 the total carry forward sales was 54649 shares with a net sale of 5207 shares. The enquiry officer observed that the member had covered the carry forward short sale in Settlement no. No.1050. The Enquiry Officer found that this was expected of a short seller who sells the shares with the hope that the prices will fall in future and buys them at a later date when the share prices have come down. In the above instance the member was having carry forward sales in SSI from Settlement no. 1047 to 1049 and the counter veiling purchase position was created in settlement no. 1050 when the price of the scrip had fallen.
  5. In the scrip of Wipro, the Enquiry Officer observed that the member had net sales in the settlement no.1047 to 1049 and the carry forward sales position has also increased from 15000 shares to 50283 shares. The total carry forward position became nil in settlement 1051 by covering short sales. It was also noted that after being a consistent seller and having significant carry forward sales from settlement no.1047 to 1050, the purchases were made in settlement no. 1051 for covering short sales.
  6. In the scrips of SBI, MTNL & Infosys, The Enquiry Officer found that the trading by the member including short sales, carry forward of short sales in these three scrips between mid Feb to mid March in an overall view of the situation do not show a tendency to artificially depress the prices in these scrips.
  7. In the scrip of Zee Telefilms, the Enquiry Officer observed that in Settlement No.1046, the member had a net sale position of 195655 shares, which constituted 7.60% to the exchange net.
  8. In the scrip of Sterlite Opticals, the Enquiry Officer observed that only one single position was maintained. There was very low trading indicating that there is no intention of FGSB to deal in that scrip.
  9. With regard to exceeding the exposure limit in the Stock exchange, the enquiry officer accepted the argument of the counsel that there was no scope for exceeding the exposure limit in the stock exchange when there is in built safeguards in the electronic system which does not permit a member to exceed the trading exposure limits.

10. With regard to cancellation of sell orders, the enquiry officer observed that, the quantity of orders are disclosed to the market and this would influence the prospective buyers and sellers to take a view on the market depending on the supply of securities. However, in the instant case there are only seven instances in three days and in two instances there is part execution of orders. The quantity of these cancelled orders are also not significant so as to give an impression that the member was trying to manipulate the share prices by such cancellation. Therefore, the charge that FGSB has cancelled sell orders in order to manipulate the share prices in the instances cited is not established.
4. With regard to trading of the member at BSE and NSE on specific dates i.e., 23<sup>rd</sup> February, 1<sup>st</sup> March and 2<sup>nd</sup> March, 2002, Enquiry Officer had given the following findings-
1. In the scrip of Satyam Computers, the Enquiry Officer observed that, FGSB had a purchase position of 15000 shares as on 26<sup>th</sup> February 2001, whereas the charge against FGSB had indulged in substantial sale with a view to artificially depress the market.
  2. In the scrip of HFCL, the enquiry officer observed that, FGSB had a cumulative net sale position of 15000 shares as on 19<sup>th</sup> February, 2001 and cumulative buy position of 40000 shares on 17<sup>th</sup> February, 2001. There is unwinding of long positions by the member. Enquiry Officer has remarked that FGSB had net sales of 34,997 shares on 2<sup>nd</sup> March, 2001. In regard to members trading at NSE, the Enquiry officer mentioned that the member had net sale of 1,16,190 shares on 1<sup>st</sup> March, 2001, which was not explained by the member.
  3. In the scrip of DSQ Software at BSE, short sales of FGSB increased by 25,000 shares on 28<sup>th</sup> February, 2001 and the purchase of 75,000 shares on 1<sup>st</sup> March, 2001 relates to covering of earlier short sales. The member had made further short sales on 2nd March, 2001 to the extent of 25,000 shares. At NSE the member had net sale of 2,55,300 shares (of which proprietary sale of 2,25,000 shares pertains to Vruddhi) which is significant.
  4. The Enquiry Officer had also examined the trading pattern of FGSB in the scrip of Infosys, MTNL, Reliance and SBI in detail.
  5. In the scrip of Wipro, the Enquiry officer had observed that, FGSB had consistently increased short sales in the scrip from Feb 17- March 02, 2001. The peak short sale of the member was 62,583 shares on 27<sup>th</sup> February, 2001. It was also observed that there was cumulative position of 60,083 shares at BSE and 24,455 shares at NSE as on 2<sup>nd</sup> March, 2001.
  6. In the scrip of Zee Telefilms, the Enquiry Officer had observed that there was a net sale of 135196 shares on 23<sup>rd</sup> February 2001 at NSE, which constitutes only 2.32% of the market net.
  7. In the scrip of Global Tele, the Enquiry office had observed that the member had net sale position of 1,35,622 shares after giving due allowance to arbitrage trades at NSE on 1<sup>st</sup> March, 2001.
  8. In the scrip of Digital Equipment, the Enquiry Officer observed that, FGSB had bought 40,180 shares at NSE on 2<sup>nd</sup> March, 2002, on account of short covering.
5. With regard to the depressing price of the scrips by FGSB, the enquiry officer observed that, the net sales during mid February and mid March is significant when compared with the net sales at the exchange. The net sales by the member cannot be compared with the trading volumes since it contains gross sales. Enquiry Officer observed that any such comparison would not lead to correct conclusions. Enquiry Officer concluded that sales in the aforesaid instances had resulted in artificially depressing the share prices. Enquiry Officer had also observed that It is not possible in such a situation where there is substantial market fall to determine with mathematical precision the amount of fall in share prices caused by a series of actions over a period of time by a market participant. Overall view of the market and the trading behaviour of the member under the circumstances during the relevant period has to be taken into account. In this connection, the carry forward sales by the member at BSE in the following scrips as a percentage of total carry forward in the exchange was taken into consideration by EO -

| Settlement no. | Scrip Name        | Sales carry forward at BSE | FGSB Sales Carried Forward | % of FGSB sales carry forward to exchange |
|----------------|-------------------|----------------------------|----------------------------|-------------------------------------------|
| 48             | Satyam Computers  | 508858                     | 85075                      | 16.72%                                    |
| 46             | SSI Ltd.          | 45283                      | 10596                      | 23.40%                                    |
| 47             | SSI Ltd.          | 78170                      | 50010                      | 63.98%                                    |
| 48             | SSI Ltd.          | 78569                      | 49000                      | 62.37%                                    |
| 49             | SSI Ltd.          | 142840                     | 54649                      | 38.26%                                    |
| 46             | Sterlite Opticals | 46296                      | 27489                      | 59.38%                                    |
| 47             | Sterlite Opticals | 40911                      | 25000                      | 61.11%                                    |
| 48             | Sterlite Opticals | 57179                      | 25000                      | 43.72%                                    |
| 47             | Wipro             | 161129                     | 15270                      | 9.48%                                     |
| 48             | Wipro             | 124133                     | 37783                      | 30.44%                                    |
| 49             | Wipro             | 131076                     | 50283                      | 38.36%                                    |
| 50             | Wipro             | 71016                      | 28300                      | 39.45%                                    |

The charges of short selling, carry forward sales, unwinding of previously built long positions were examined by the Enquiry Office in the light of submissions made by the member. The Enquiry Officer had given allowance to the arbitrage positions and the other trades, where the member had significant buy positions and errors in the data. The Enquiry Officer also observed that the member had not exceeded the carry forward sales limits of the exchanges. The percentage of carry forward sales of the member against the total carry forward sales at BSE is high in the relevant period in the scrips of Satyam, Software solutions, Sterlite Optical and WIPRO. Though short sale is a permitted activity what is to be seen is whether the trading behaviour of the member between mid Feb and mid March in the select scrips has contributed to artificial depression of the share prices. The Enquiry Officer had found that the overall trading by the member during the aforesaid period has contributed for the fall in share prices.

6. With regard to order placement in specific time slots by FGSB, the Enquiry officer has found that out of 9 transactions involving sale of shares by FGSB during specific time bands impacting the share prices, on the specific dates, three instances involving the sale of Wipro at BSE on 23<sup>rd</sup> February and 27<sup>th</sup> February, 2001, the short sale by the member during the specific time slots were examined. No evidence was forthcoming for the last 3 transactions involving sale of Wipro at NSE on 1<sup>st</sup> March and 2<sup>nd</sup> March, 2001. In other 3 transactions, there is no sufficient evidence to establish the charge. Therefore, the EO concluded that the charge was established to the extent of three transactions as stated above.
7. With regard to charge that there was circular trading and routing proprietary trades through unregistered entities, Enquiry Officer has stated that the member had dealt with Palombe Securities which is an unregistered sub-broker. Relying on the statement of Bhaskar Hingad dated 3<sup>rd</sup> August 2001 who stated that Palombe Securities would be responsible for payments to Bang Equity in case of default, enquiry officer came to this conclusion. This is as it should be between a sub-broker and a broker. Enquiry Officer found that, the fees received by Palombe from Bang is more than mere introductory fees because he is also undertaking the liability in case of a client's default. Therefore, Enquiry Officer found that FGSB was dealing in securities through an unregistered sub-broker which is unbecoming of a registered stockbroker.
  1. With regard to charge that FGSB indulged in synchronised trades, the Enquiry officer noticed that the transactions between FGSB & Bang Equity were synchronized transactions in view of the close proximity of the order time punched by both the parties in the system. He found that both the firms had entered buy and sale orders for the same quantity of shares almost simultaneously. There is no transfer of title in these shares since the purchase and sale quantity are exactly the same. For the matched trades, the difference in time space is as little as just a second in the case of Sterlite on 1<sup>st</sup> March, 2001 for 50,000 shares. While in some cases, there was 100% matching of the buy and sale quantity, in other cases, majority of the order quantity got matched. The more the gap between the order timings, the less it is likely to get matched and vice-versa. The value of such transactions is also quite high. Enquiry Officer concluded that such transactions defeat the very purpose of normal order-matching system in the price discovery process in the exchanges and are in violation of Regulation 4(c) & (d) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to securities market), 1995
  2. With regard to FGSB acting in concert, Enquiry Officer concluded that Vruddhi, FGSB and Bang Entity were acting in concert with each other in the synchronized deals.
8. With regard to FGSB transactions with RNA Group, it was found by the EO that the absorption of losses on account of arbitrage trading for RNA group by FGSB would amount to guaranteeing no negative return which is not in compliance with Regulation 14(3) of SEBI (Portfolio Manager) Regulations.

## **5. Enquiry Officer Report on the Show Cause Notice dated 6<sup>th</sup> October, 2001.**

1. With regard to charge that FGSB has indulged in sales which are not in compliance with SEBI Circular dated 7<sup>th</sup> March, 2001, Enquiry Officer found that FGSB had undertaken short sales in securities after 8<sup>th</sup> March, 2001, which is not in conformity with the aforesaid Circular of SEBI and the quantum of such short sales are also quite high.
2. With regard to charge that FGSB had shown some of the trades executed by them as institutional trades though they were not institutional trades and thus evaded payment of margin money in respect of these transactions and by excluding these trades while calculating gross exposure and intra-day trading limits, the member had over- stretched trading limits, the Enquiry Officer found that the charge relating to evasion of margins by FGSB by showing certain trades as institutional trades though they were not institutional trades and thereby avoiding payment of margins, etc. has been established.
3. With regard to charge that, FGSB had not co-operated in the ongoing investigations into the irregularities regarding stock market volatility and even summons issued for furnishing of information were not complied with, the Enquiry Officer found that as member had failed to furnish information to SEBI and did not cooperate with the investigation officer and even the summons issued in this connection were not responded, the charge of non cooperation including furnishing the information to the Regulator is established.

## **6.0 Recommendations of the Enquiry Officer.**

The Enquiry Officer has given the following recommendation in this report:

"The various types of misconduct including artificially depressing the share prices in the market by manipulation, on the part of the member has to be judged against the steep fall in the stock market indices between mid February and mid March 2001 with particular reference to specific dates such as 23<sup>rd</sup> February, 2<sup>nd</sup> March and 13<sup>th</sup> March where the intra day high and low prices were very sharp and the fall from the previous close were also substantial. Due to steep fall in the stock market indices which were reflected in the stocks comprising of the indices and the general fall in the prices of other scrips as set out in the show cause notice the value of the investments by public at large had eroded considerably.

Therefore, having regard to the gravity of various types of the misconduct that have been established against the member including that of artificially depressing the prices in the securities in select scrips has detailed in the preceding pages, I recommend that the certificate of registration granted to First Global Stock Broking Pvt. Ltd. as stock broker and portfolio manager be cancelled. It is also recommended that the certificate of registration granted to Vruddhi Confinvest India Pvt. Ltd. as sub-broker be cancelled. These recommendations are made under Regulation 13 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Markets) Regulation 1995 for consideration by the Board in terms of Regulation 28(7) of SEBI (Stock Brokers and Sub-brokers) Regulations, 1992 and Regulation 34(7) of SEBI (Portfolio Managers) Regulations, 1993. "

#### **0. Show Cause Notice issued by the Board**

1. A Show Cause Notice dated 10<sup>th</sup> January 2002 was issued to FGSB and VCIP together with copy of the Enquiry Officers' Report asking them to show cause as to why the penalty as considered appropriate by the Board should not be imposed.

#### **0. FGSB and VCIP reply to the show cause notice**

1. DH Law Associates have vide their letter dated 24<sup>th</sup> January 2002 submitted their reply to the show cause notice containing findings of Enquiry officer and his recommendation. In their reply, they have, inter alia, stated as under :-
2. It was stated by the FGSB that they had been denied diverse records of documents necessary for defending themselves. FGSB has never been given an opportunity to cross check the correctness of the data used against it. The following instances were quoted by the FGSB :

(i) The underlying data for computing net sales of the exchange has not been produced.

ii) Data in the charges relating to NSE trades has been completely ignored by the Enquiry Officer.

iii) Copy of letter dated 03.10.2001 from SEBI to BSE asking for authenticated data has not been furnished.

iv) Data regarding time slots has not been explained. The time slots have been changed in Show Cause Notice from that in Preliminary Investigation Report.

7.2 The Preliminary Investigation Report. (PIR) – FGSB submitted that they were entitled to a full copy of PIR and that this was suppressed. The PIR contained many details all of which militated against the charges made. It was stated that the PIR given to FGSB did not contain such details as – i) reasons for continuous market fall do not relate to FGSB. ii) Reasons for market behaviour. iii) Institutions such as UTI were behaving same as FGSB. iv) Lack of correlation between any of the charges and price movements.

It was further submitted that the extract given to FGSB as an extract from PIR was a doctored document which had been tampered with and that it contained material and substantial changes, designed to meet the argument of FGSB.

3. With regard to time slots FGSB submitted that each of the time bands were time bands when the orders were executed on the exchange and not the time of placement of orders. The Enquiry Officer recorded that these charge actually means order execution time. The data did not support the charge as made. The order placement charge did not survive and stood substituted by a charge of order execution in specific time slots when its scrip prices registered substantial fall. FGSB had no control over execution times. The Enquiry officer proceeded against FGSB on the charge of order placement, which even the presenting officer says does not exist. Since, data dealt with Enquiry officer is admittedly order execution times and the Enquiry Officer had other data , there is absolutely no way the Enquiry Officer could have held that any charge of order placement had been proved.
4. With regard to charge of violation of Portfolio manager Regulations in the transactions for RNA Builders – FGSB submitted that RNA Builders had deposited monies with FGSB for arbitrage trading. It was further submitted that sometimes on the instructions of RNA, there would be non-arbitrage trades, which would result in delivery to clients. No Portfolio of shares was ever held by FGSB and none is shown or even alleged. The said transactions were arbitrage transactions but not portfolio transactions. It was submitted by FGSB that arbitrage transactions require full delivery being taken on one exchange and full delivery being given on the other. Therefore fund to the extent of the transactions are usually kept with the broker. FGSB contended that a finding that this was portfolio management must require a finding that these were not arbitrage trading. It was submitted that these very transactions were pointed out as arbitrage transactions and excluded whilst computing the sell trades of FGSB, on the basis that since these were arbitrage trades, they had corresponding buys on the other exchange. The transactions cannot change their character to non – arbitrage. FGSB alleged that this was done as a deliberate dishonest twist for the purposes of making a finding against FGSB. The Sauda Error Accounts did not absorb losses but absorbed wrong/erroneous trades. The errors may result in profit or loss. It was recorded by the Enquiry Officer in the daily proceedings sheets that the submission was that Sauda Error does not absorb losses but only errors.

5. With regards to Matched Trades – FGSB submitted that there was no charge of matched trades. The charges had always been vague and imprecise, sometimes being referred to as 'synchronized trading' sometimes circular trading, sometimes negotiated deals and sometimes 'fictitious trades'.
6. FGSB further submitted that the reason for the trades were fully explained that it was done in close proximity to avoid potential loss. These trades were all through the exchange's price discovery systems.
7. On the trading pattern FGSB submitted that the Enquiry Officer made specific findings in respect of at least four scrips (MTNL, INFOSYS, SBI, Sterlite Opts) that there was no bearish pattern or intent to hammer. Nevertheless, on trading in specific days, he makes adverse notings. Whilst the show cause notice itself sets 5% or more as being heavy sales, the Enquiry Officer has ignored them and made adverse remarks when the sales were as low as 1.79% to the exchange net.
8. With regard to the Cumulative Table – The FGSB gave their own data for 22 days involved showing that on 11 days they were net buyers and on 11 days they were net sellers. The FGSB data had, in the 22 days discrepancies from earlier data submitted. The FGSB were net buyers on those days. In the very chart, the FGSB were net buyers on 14 days out of 23.
9. With regard to Carry forward FGSB contended that the Presenting Officer introduced a new data/charge of heavy carry forward during the hearing. There is no charge in relation to the scrip of SSI. Yet the Enquiry Officer proceeds to give finding on that scrip. Further, he never pointed out that this scrip was a relevant consideration.
10. On the Fraudulent and Unfair Trade Practices Regulations, FGSB submitted that the hearing under Reg.13 has been held without a report under Reg.10 or any hearing under Reg. 11 and any findings. The hearing under Reg. 13 read with Reg. 29 of the SEBI (Stockbroker and Sub broker) Regulations, was therefore illegal and void. In any event, it could not proceed without the conditions precedent being met.
11. On 6<sup>th</sup> October show cause notice, FGSB contended that this notice was bad in law as the Enquiry Officer was never even appointed. His appointment is limited to the terms of his appointment order.

## 7. Hearing before the Board

A oral hearing was granted to FGSB and VCIP before the Board on 29<sup>th</sup> January, 2002. Meantime FGSB filed Writ Petition No.71/2002 on 22<sup>nd</sup> January, 2002 before Hon'ble Bombay High Court. FGSB replied to the show cause notice on 24<sup>th</sup> January, 2002 as stated above contending that the enquiry report stood vitiated and the Chairman, SEBI being a party to the above writ petition could not hear the matter. When the said petition no.71/2002 came up for admission for interim relief, FGSB applied for leave to withdraw and sought liberty to file fresh petition. The Writ Petition (L) no.304/2002 was filed on 28<sup>th</sup> January, 2002 i.e. the day before FGSB appeared for hearing before the Board.

8.1 FGSB and VCIP appeared before the Board along with their counsels on 29<sup>th</sup> January, 2002. The then Chairman, SEBI, Shri D R Mehta recused himself from the proceedings in view of the personal allegations made against him by FGSB and associates.

2. In the hearing before the Board on 29<sup>th</sup> January 2002 FGSB contended that the hearing on the said date should be deferred till the out come of the Writ Petition (L) No. 304/2002. It was stated by the Board that hearing might continue and complete that day and orders would be reserved till the date of hearing of the above petition. Accordingly the hearing was held. During the course of hearing, FGSB and VCIP reiterated the submissions made in their reply to show cause notice.
3. The petition came up for admission on 31<sup>st</sup> January 2002 before the Division Bench of the Hon'ble High Court of Mumbai comprising Justice AP Shah and Justice V K Tahilramani. Advocate General appearing for SEBI made a statement that SEBI would not pass orders till 14<sup>th</sup> February 2002. In view of the said statement the Hon'ble Court was pleased to order that the interim order dated 25<sup>th</sup> May 2001 will continue till then. The said interim orders were extended from time to time.
4. The Hon'ble High Court was pleased to dismiss the above writ petition vide its orders dated 11<sup>th</sup> April 2002 with the following directions:
  - i. In response to the notice dated 10<sup>th</sup> January 2002, the petitioners no.3 and 4 (FGSB and VCIP) shall be at liberty to file comprehensive additional reply within two weeks from today.
  - ii. Upon receipt of the additional reply from petitioners' no. 3 and 4 the respondent no.1 - SEBI Board shall fix date/s of hearing expeditiously and preferably within two weeks from the date of receipt of additional reply.
  - iii. All contentions raised by the petitioners no. 3 and 4 in the writ petition and which have been raised in the reply already submitted or in the additional reply that may be submitted by them, are kept open to be considered on their own merits by respondent no.1 - SEBI Board uninfluenced by any statement made in the reply affidavit or withdrawal of earlier writ petitions or dismissal of this writ petition in limine.
  - iv. In case any adverse order is passed by respondent no.1 - SEBI Board against the petitioners no. 3 and 4 such order shall remain stayed for a period of four weeks from the receipt of the copy of the order by them.

v. The order passed under Section 11B of SEBI Act, 1992 on 25<sup>th</sup> May 2001 shall remain operative as regards petitioners no.3 and 4 till the order is passed by respondent no.1 - SEBI Board and in case adverse to the said petitioners for four weeks thereafter.

2. Accordingly FGSB furnished their reply afresh vide its letter dated 26<sup>th</sup> April 2002 and Board has fixed a hearing on 14<sup>th</sup> May 2002 at Delhi. FGSB appeared before the Board on the said date of hearing and made submissions. At the end of the day the counsel of FGSB requested for additional time to present their case before the Board. Accordingly another hearing was granted to FGSB on 24<sup>th</sup> June 2002 at SEBI Head Office, Mumbai as requested by them. DH Law Associates vide its letter dated 15<sup>th</sup> May 2002, stated that they had no objection to the delay in the next hearing date with reference to the 14 day time referred to the Hon'ble High Court's order.

3. The counsel of FGSB and VCIP appeared for the hearing on 24<sup>th</sup> June 2002 and resumed their submissions. During the hearing it was pointed out to the counsel that the submissions were repetitive. The counsel replied that, that this his style of arguing the matter. At the end of hearing the counsel appearing for FGSB stated that his submissions were not yet completed and sought for another date of hearing. The Board directed the counsel to complete the oral submissions and submit written submissions including any issue, which was not covered in the oral hearings within 10 days. The Board assured FGSB and VCIP that they will duly consider all submissions of FGSB before passing the order. They agreed to file the written submission within the given time.

4. Subsequently, D H Law Associates the advocates for FGSB had sent a letter to SEBI dated 20<sup>th</sup> June, 2002 (which was received on 25<sup>th</sup> June, 2002) wherein it was mentioned that they would require atleast two days or more for full hearing on all aspects.

5. SEBI had received one more letter dated 24<sup>th</sup> June, 2002 from D H Law Associates on 26<sup>th</sup> June, 2002. It was mentioned in the said letter that "Although the counsel's presentation has remained in conclusive, the Board chose to close the hearing at 5.45 PM" It was also stated that "Even if our clients decide to file written submissions as suggested by you, it will not be as substitute for a proper oral hearing".

6. A clarification dated 26<sup>th</sup> June, 2002 was issued to D H Law Associates that on receipt of FGSB written submissions, if there is any issue which had not been submitted by them before the Board, the Board would consider the issue of giving an oral hearing on those issues.

7. In response to the said letter, D H Law Associates in their letter dated 3<sup>rd</sup> July, 2002 without filing the written submissions requested the Board to consider their request and grant them further hearing in the matter in the interest of Justice and Equity.

8. Upon receipt of the letter from D H Law Associates another letter was issued to D H Law Associates, reiterating the contents of the letter dated 26<sup>th</sup> June, 2002 and indicated that if they do not avail the opportunity of furnishing written submissions within a week from receipt of this letter, the Board would be constrained to proceed further in the matter with the material available on record and the submissions made by them hitherto.

9. In this said letter dated 25<sup>th</sup> July, 2002 a further personal hearing was granted to FGSB on 2<sup>nd</sup> August, 2002 and it was advised that FGSB should submit their written submissions. FGSB was asked to confirm their attendance for the hearing within two days of receipt of the said letter. FGSB did not confirm the same till 1<sup>st</sup> August, 2002

10. On 1<sup>st</sup> August, 2002 a letter dated 30<sup>th</sup> July, 2002 was received from D H Law Associates. The letter, inter alia, stated that :

- The hearing was concluded by the Board on 24<sup>th</sup> June, 2002 and their several requests for a full hearing went unheeded.
- Now the Board is functus officio, it appears that the Board wish to revive the hearing., This cannot be done and they referred to a case of M J Patel v/s SEBI before Securities Appellate Tribunal, Mumbai.
- They also referred Regulation 29 of SEBI (Stock Brokers and Sub Brokers) Regulations, 1992. Section 29(3) of the said regulation stated that "The Board after considering the reply to the show cause notice if received, shall as soon as possible but not later than thirty days from the receipt of the reply, if any, pass such order as it deems fit. The letter also stated that " without prejudice more than 30 days have passed from the closure of the hearings".

2. On 14<sup>th</sup> August 2002, DH Law Associates wrote on behalf of FGSB and VCIP stating that they have not been given a notice of Board meeting held on 9<sup>th</sup> August 2002. They contended that such purported hearings without notice are illegal and void. They once again reiterated their letter dated 30<sup>th</sup> July 2002 and requested to reactivate their clients trading terminals.

3. The Board through its solicitors M/s Maneksha and Sethna wrote a detailed letter on 22<sup>nd</sup> August 2002 to DH Law Associates inter alia, calling upon them to categorically state whether their clients wanted to file written submissions or not as directed by the Board, failing which the Board will proceed to consider the case on the basis of the present record.

4. DH Law Associates vide its letter dated 27<sup>th</sup> August 2002 to M/s Maneksha & Sethna replied to letter dated 22<sup>nd</sup> August 2002, inter alia, reiterating their stand.

5. FGSB and VCIP neither availed the opportunity of further oral hearing granted by the Board nor filed their written submissions.

6. In view of the above, the present order is passed basing on and taking into consideration the material available on record including Enquiry Officer Report dated 9<sup>th</sup> January 2002, FGSB and VCIP's reply dated 24<sup>th</sup> January 2002 to the Show cause notice, additional comprehensive reply pursuant to the order of Hon'ble High Court and submissions made on behalf of FGSB and VCIP during the hearings dated 14<sup>th</sup> May 2002, 24<sup>th</sup> June 2002 and their letters dated 25<sup>th</sup> July 2002, 01<sup>st</sup> August 2002, 14<sup>th</sup> August 2002 and 27<sup>th</sup> August 2002.

## **9.0 Consideration of the Issues**

### **1. Whether the differences in PIR & Draft PIR vitiate the enquiry proceedings?**

1. The contention of FGSB was that there are differences in the PIR as submitted by the Union of India before the Justice Venkataswami Commission and the one Enquiry Officer gave to FGSB in October 2001. FGSB attributed malafides on the Board and the former Chairman for the said reason. Board has taken a serious note of the said allegations of malafides and examined the PIR as submitted to the Justice Venkata Swami Commission and the one given by the Enquiry Officer to FGSB and Associates in October 2001.
2. It is observed that Securities and Exchange Board of India has prepared only one PIR and submitted to the Government. As far as SEBI is concerned this is the PIR. It is further observed that it was the only PIR that SEBI prepared as far as FGSB is concerned. The presenting officer in the sworn affidavit filed in writ petition no.824 / 2002 had explained that "while the enquiry proceedings were going on a copy of relevant part of the PIR was printed afresh from the computer soft copy and was handed over to the enquiry officer. This copy later turned out to be a part of the draft version of PIR before finalization of the same".
3. We have also noted that it is not necessary for the Board to furnish a full copy of the investigation report to FGSB but only relevant portion of the findings of the investigation and the documents relied on need to be communicated. In any case all the charges were appropriately framed and communicated by the Enquiry Officer to FGSB and Associates. FGSB and Associates has also replied to the charges mentioned in the Show Cause Notices. We also have carefully looked into the differences in the draft PIR and PIR submitted to the Government and find that the differences do not have impact on the charges against FGSB and others.
4. We have also noted that the enquiry officer has relied on the material made available to him and communicated the same to the FGSB and others as a part of enquiry proceedings. Therefore, FGSB and others were in no way prejudiced by the said differences. In any view of the matter FGSB had copy of the PIR. Otherwise they would not have been able to compare the same. This is not a case where FGSB was not aware and did not have a copy of the material relied on. FGSB right from the beginning, as observed above was trying to point out minor errors to gain advantage out of it. FGSB is virtually trying to create mountains out of mole hills by exaggerating trivial matters which do not have any bearing on the proceedings. This attitude of FGSB and others has unnecessarily resulted in delaying the proceedings.

### **9.2 Whether proceedings are in violation of FUTP Regulations?**

We have gone through the submissions of FGSB in regard to SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995:

1. Regulation 10 envisages a report being made after considering the party's submissions. This report is a final report on the investigation. The hearing mentioned in Regulation 11 is final in as much as final orders are then passed under Reg.12 (Reg.13 is optional and in its own nature is a final order or direction under Reg.11). At this stage, a party fully knows the case he must meet, the basis of the charges, SEBI's final views on the investigation and all aspects. The party will then be in a position to meet the full case and in the circumstances, a final hearing is contemplated under Reg.11.
2. FGSB submitted that as on 25<sup>th</sup> May 2001 when enquiry had been ordered, the investigation was not complete, no final report had been submitted and even toady only an interim report has been submitted. No final investigation report envisaged in Reg. 10 which form the basis of the hearing under Reg. 11 has been submitted or produced. Even the preliminary investigation report, which is the sole basis of the enquiry, was furnished only in the course of the current hearing.
3. It was further stated that there is a further interim investigation report which has not been furnished. As on date, it is not even known whether investigation has been completed. The hearing for S.11B cannot therefore be equated to a hearing under Reg.11.

4. It was submitted that since Reg.11 is a final order in itself, the findings therein on the charges under FUTP will be final. The Enquiry Officer cannot make a fresh enquiry into those findings or into any charges under the FUTP Regulations when acting under Regulation 13. Regulation 13 is only reiterates the compliance with the requirements of the regulations applicable to the intermediary in case suspension or cancellation is contemplated. In considering this, the Enquiry Officer must only look to the findings under Reg.11. It was stated that in the instant case, since there are no such findings, the Show Cause Notice must be discharged.
5. FGSB submitted that Regulation 12 orders are final orders and must be passed on final findings. Similarly, the order appointing an Enquiry Officer under Reg. 13 is only after coming to a final decision that the breaches of FUTP are such as to justify proceedings for cancellation or suspension and does not follow a Reg.11 order as a mere formality. Appointment of an Enquiry Officer under Reg.13 is a decision that must be judiciously taken under Reg. 11.
6. FGSB has further submitted that alternatively, if there are two hearings (Reg.11 and Reg 13 with potential of two independent penalties (Reg.12 and 13 if there are two proceedings), the proceedings are in the nature of double jeopardy and the regulations are violative of Art.20 of the Constitution of India (since proceedings are quasi criminal and involve punishment for purported offences.)
7. We have examined the above arguments of FGSB with regard to non compliance of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995. The scheme of the regulations is as under:
8. Under Regulation 7 of the said regulations the Board is empowered to investigate into any allegation of Fraudulent and Unfair trade Practices. The said regulation reads as under:
  7. (1) The Board may, suo-moto or upon information received by it, cause an investigation to be made in respect of the conduct and affairs of any person buying, selling or otherwise dealing in securities, by an investigating officer whom the Board considers fit.

Provided that no such investigation shall be made except for the purposes specified in sub-regulation (2).

(2) The purposes referred to in sub-regulation (1) are the following, namely-

(a) to ascertain whether there are any circumstances which would render any person guilty of having contravened any of these regulations or any directions issued thereunder;

(b) to investigate into any complaint of any contravention of the regulation, received from any investor, intermediary or any other person; Under Regulation 8 a procedure for investigation has been stipulated and a notice is prescribed which can be dispensed with by the Board at its discretion. The said regulation reads as under:

#### Procedure for investigation

8. (1) Before causing an investigation to be made under Regulation 7, the Board shall give notice.

(2) Notwithstanding anything contained in sub-regulation (1), where the Board is satisfied that in the interest of the investors or in the public interest, no such notice should be given, it may, by an order in writing and recording the reasons as far as practicable, direct that the investigation be undertaken without such notice.

(3) Subject to the provisions of this regulation, an order passed under regulation 7 shall be a sufficient authority for the Investigating Officer to undertake the investigation and, on production of an authenticated copy of the order, the person concerned shall be bound to carry out the duty imposed in regulation 9.

Under Regulation 10 of the said Regulation the investigating officer submits his report to the Board and the Board is entitled to pass any direction under Reg. 11 depending upon the circumstances of each case. The said Reg. 10 and 11 are as under:

#### Submission of Report to the Board

10. The Investigating Officer shall, on completion of the investigation, after taking into account all relevant facts and submissions made by the person concerned, submit a report to the Board.

#### Power of the Board to issue directions

11. The Board may, after consideration of the report referred to in regulation 10 and after giving reasonable opportunity of hearing to the person concerned, issue directions for ensuring due compliance with the provisions of the Act, rules and regulations made thereunder, for the purposes specified in regulation 8.

The following directions can be passed by the Board :

Purpose of directions  
12. The purposes for which directions under regulation 11 may be issued are the following, namely -

- (a) directing the person concerned not to deal in securities in any particular manner;
- (b) requiring the person concerned to call upon any of its officers, other employees or representatives to refrain from dealing in securities in any particular manner;
- (c) prohibiting the person concerned from disposing of any of the securities acquired in contravention of these regulations;
- (d) directing the person concerned to dispose of any such securities acquired in contravention of these regulations, in such manner as the Board may deem fit, for restoring the status-quo ante.

However, in case of intermediaries a separate procedure has been prescribed for imposing penalties. Under Sec. 12(3) of the SEBI Act, a registration of an intermediary cannot be suspended or cancelled without giving the said intermediary an opportunity of hearing. SEBI has framed various Regulations for various intermediaries. If any intermediary has prima facie found to have violated FUTP regulations his registration can either be cancelled or suspended after following the procedure under the respective regulations concerning the intermediary. The regulation reads as under: Suspension or cancellation of Registration<sup>13</sup>. The Board may, in the circumstances specified in regulation 11 and without prejudice to its power under regulation 12, initiate action for suspension or cancellation of registration of an intermediary holding a certificate of registration under section 12 of the Act.

Provided that no such certificate of registration shall be suspended or cancelled unless the procedure specified in the regulation applicable to such intermediary is complied with.

9.2.9 It is clear from the provisions of the above regulations that on completion of the investigation a report has to be submitted to the Board. The Board has to then decide whether directions under regulation 12 of the nature specified in regulation 12 should be issued and / or it wishes to suspend or cancel the registration of an intermediary. If the Board decides to pass the directions of the nature specified under regulation 12, it has to follow the procedure under regulation 11.

10. If the Board decides to suspend or cancel the registration of an intermediary the Board, need not comply with Regulation 11 and 12 but under regulation 13 is required to follow the procedure with the regulations applicable to the intermediary concerned which in this case is SEBI (Stock Brokers and Sub-brokers) Regulations, 1992 and SEBI (Portfolio Managers) Regulations, 1993. In the event of the Board deciding to pass both directions under regulation 12 and cancel or suspend the registration, it is required to grant a hearing, which hearing can always be combined with the hearing under the regulations applicable to the concerned intermediary. Therefore, in the facts and circumstances of the case we are of the view that no hearing was necessary in terms of regulation 11 at that stage. We are satisfied that the provisions of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995 and SEBI (Stockbrokers and Sub-brokers) Regulations, 1992 are fully complied with. In any view of the matter FGSB and associates were given an opportunity of hearing by the Chairman, SEBI on 18<sup>th</sup> May, 2001 before the appointment of Enquiry Officer.
11. In the present case FGSB is a stock broker and Vruddhi Confinvest India Pvt. Ltd. is a sub broker, both are registered under SEBI (Stockbrokers and Sub-brokers) Regulations, 1992. Therefore, an enquiry officer has been directly appointed under SEBI (Stockbrokers and Sub-brokers) Regulations, 1992 and SEBI (Portfolio Managers) Regulations, 1993 to conduct the enquiry as per the procedure laid down there for the violations of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995.

### **9.3 Whether all the documents have been furnished to FGSB and VCIP**

We have perused the show cause notices, the annexures and documents, findings of investigations annexed to the show cause notices and also the proceedings of enquiry. We find that the following information /documents /tables have been furnished to FGSB and other entities. –

on 24<sup>th</sup> April, 2001 : Investigation report read in front of the officials of First Global Stock Broking Pvt. Ltd. namely Mr. Shankar Sharma, Ms. Devina Mehra, Mr. Neeraj Khanna and Mr. S.S.Dhillon and copies of relevant documents were obtained.

On 8<sup>th</sup> May, 2001:

- Copies of 19 tables (tables were given in the preliminary investigation report submitted to Ministry of Finance on 14<sup>th</sup> April, 2001).
- Copies of loose papers (which were selected by Mr. S.S.Dhillon and Mr. Neeraj Khanna after inspecting 6 files) which runs about 124 pages. The papers contain the following information-
- List of top 20 clients (on the basis of turnover during for month of Feb 2001) (1 page)
- List of FGSB group accounts (3 pages)
- Securities lending /borrowed forms –SHCIL (17 pages)
- Ledger copy of Sahara India Financial Corporation and B.N.Prakash (2 page)

- Party code list – starts with letter "U" (3 pages)
- Order /confirmation messages and contract notes/ for the client "Battery March" (98 pages)

#### On 12<sup>th</sup> September 2001

- Statement of Roshanlal Agarwal of RNA Group
- Statement of Nirmal Bang
- Statement of Bhaskar Hingad of Palombe Securities
- Stock Lending form

#### On 6<sup>th</sup> October 2001

- Exchange authenticated data on Net position at the exchange in the scrips & settlements, dates and time slots mentioned in the show cause notice.
- Exchange authenticated data on Cumulative table (table no. 6 of Show Cause Notice).
- Exchange authenticated data on matched/ synchronised trades.

#### On 16<sup>th</sup> October , 2001

- Statement of Bhaskar Hingad
- Copy of the PIR so far related to FGSB.

#### 19<sup>th</sup> October 2001

- Copy of statement of Shri Shankar Sharma dated 4<sup>th</sup> March 2001

#### 1<sup>st</sup> November , 2001

- NSE letter on market net in the scrips & settlements, mentioned in the show cause notice.

#### 19<sup>th</sup> November, 2001

- NSE letter on market net in the scrips & time slots mentioned in the show cause notice.

#### 22<sup>nd</sup> December 2001

- Floppies containing trade logs of BSE & NSE pertaining to arbitrage transaction of RNA Group

#### 1<sup>st</sup> January 2002

- Details of FGSB trades which were not in compliance with SEBI circular dated 7th March, 2001. on restricting of short sale ( Details of CA Report)

We further found that FGSB had made wild allegations without precisely pointing out what documents they required and what had not been furnished to them. The Enquiry Officer in his letter dated 16<sup>th</sup> October 2001 had clearly indicated that FGSB should illustrate how each and every document is relevant to the charges and to the enquiry being held against them and whether and how their non-supply would prejudice their case.

Therefore we find that all the necessary documents and records relied on or referred to in the show cause notice have been duly furnished.

#### **4. Whether the FGSB and VCIP artificially depressed the share prices.**

1. In the scrip of Global Tele , Enquiry Officer observed that there was a net sale of 89350 shares in settlement no 1050. FGSB stated that Enquiry Officer ignored the creation of the long position and submitted that the majority of the sales are client sales.

We are of the view that the net sales of the member in this scrip is significant.

2. In the scrip of HFCL, the Enquiry Officer observed that in Settlement no. 48, there was a net sale of FGSB to the extent of 99,166 shares which constitutes 9.47% to exchange net and Vruddhi was holding delivery of 84,000 shares.

FGSB replied that the trading at Settlement no..48 is mentioned although there is no proprietary net sales. They further submitted that it would be absurd to suggest that prices were being depressed while holding 84000 shares. There would be no sense in simply cutting ones nose to spite ones face. There are buy positions throughout and settlement no. 48 is followed by net buys throughout.. SEBI's own data proves this figure wrong. According to SEBI, the net sales in that settlement (17/2 to 23/3) for FGSB was 55117 (not 99166) much less that the proprietary holding. There was no proprietary net sale.

We are of the view that the argument of FGSB is not correct. The charge against the FGSB was that they were using their positions to depress the prices. This aspect is substantially proved by this finding. FGSB has not showed any evidence that the sale resulted in delivery. This itself shows intentions of FGSB other than liquidating their position. The cumulative position in the table (page 11 of show cause notice dated 17<sup>th</sup> July 2001) refers to the position in the scrip from 17<sup>th</sup> February 2001. The member has raised this issue for the first time.

3. In the scrip of Satyam, the member had a net sale of 2,80,801 shares in Settlement no.1041 at BSE which is 5.60% to exchange net sales. Again in Settlement no.1043, the member had net sales of 173490 shares at BSE which is 5.44% to exchange net. These sales are significant but these settlements are prior to mid February period. In Settlement No.1045, there was a net sale of 233856 shares which constituted 7.82% of net sales of the exchange with a carry forward sale of 80000. These sales were covered in the next settlement i.e. 1046 with a Teji Badla position of 50,000 shares.

FGSB stated that the Enquiry Officer while noting that the position prior to mid February was irrelevant referred to the positions in settlement no. 1044 position (5/2 to 10/2). We are of the view that this period is relevant in view of the charge of unwinding of previously built long positions. Hence there is no question of bias in this as alleged by FGSB. The settlement no. 1048 proprietary position (i.e. on 23<sup>rd</sup> February 2001) is noted. Elsewhere however the enquiry officer noted that the net position (considering the NSE/BSE) on that date was according to SEBI +15000 shares (more according to FGSB).

On any count, FGSB were buyers overall and this position is admitted by SEBI. The adverse noting is possible only by ignoring a corresponding net 100,000 shares buy at the NSE in that scrip.

We have noted that the purchase and sale position by the member prior to mid February has not been taken into account by the Enquiry Officer since the charge relates to artificially depressing the prices in the scrip between mid February to mid March. He however, noted that the carry forward sales of 19,865 shares in Settlement no. 1044 increased to 80000 shares in Settlement no. 1045. The carry forward sales of 85000 shares in Settlement no. 1048 relate to proprietary dealings pertaining to FGSB which itself is significantly large as compared to total carry forward sales at the Exchange.

We are therefore of the view that FGSB and VCIP had contributed to substantial sale pressure in the scrip, which resulted into price fall in the scrip.

4. In the scrip of SSI, Enquiry Officer observed that there was a net sale of 10,136 shares in Settlement no.1046 at BSE which constituted 3% to the exchange. There was net sale of 39479 shares in Settlement 1047 which constituted 9.10% to exchange net and by the end of the settlement carry forward sales in the scrip settlement is 50000 shares. By Settlement no. 1048, the total carry forward sales of the member was moderately decreased to 49000 shares and in Settlement no. 1049 the total carry forward sales position went up to 54649 shares with a net sale of 5207 shares. Enquiry Officer observed that the member had covered the carry forward short sale by purchases in Settlement no. No.1050. In the above instance the member was consistently having carry forward sales in SSI from Settlement no. 1047 to 1049 and the counter veiling purchase position was created in 1050 when the prices had fallen.

On behalf of FGSB it was stated that this is complete transgression of authority / power. The enquiry was limited to 10 scrips after considering the SSI data. The Enquiry Officer had no business to ignore his superior's directive or to deal with this scrip. If an allegation was made, the Enquiry Officer had no authority to do so.

It was also contended by FGSB that the enquiry officers' finding however is of interest and defeats the charge itself. According to him, even purchases are tainted by a short sell. This cannot avoid the fact that the buy is counter trade and has counter connotations. More interestingly, he notes that the short sells are in expectation of a future fall in prices, not a fall caused by the transactions impugned but a fall in the future. This establishes the gaminess of the trades, the lack of manipulation or depression (artificial or at all) and explains SEBI failure to provide any price fall data or the Enquiry Officer's failure to consider them.

This issue has been carefully looked into and we opine that there is no transgression of Authority / Power by the Enquiry Officer. It is true that in the initial stage of investigation ten scrips were examined however as the investigation progressed, on the basis of findings other scrips were also included. The same has been reported in the Preliminary Investigation Report as well as Show Cause Notice. Hence FGSB's plea is not tenable. We find that the trading pattern of FGSB & VCIP in this scrip led to crash in the scrip price.

5. In the scrip of Wipro, the Enquiry Officer observed that the member had net sales in the Settlement no. 1047 to 1049 as above and the carry forward sales position has also increased from 15000 shares to 50,283 shares from Settlement no. 1047 to 1049. The total carry forward position became nil in Settlement no. 1051 with covering purchases. Here also it is noted that after being a consistent seller and having significant carry forward sales from Settlement no. 1047 to 1050, the covering purchases were made.

FGSB stated that this was the only scrip with some active trading and that there had been serious buys as well. Additionally, the volumes traded were nominal. It was further stated that SEBI itself found in September 2001 that this scrip was not manipulated. The findings were contemporaneous and covered the entire period

up to September 2001. We have gone through the reply of the FGSB and since the Enquiry Officer exonerated the FGSB of any manipulation on this scrip, the reply of FGSB is not relevant here.

FGSB itself accepted that the member had dealt in the scrip. We have also observed that the member had built up huge carry forward sale position around February end. The scheme of trading in this scrip and trading in the scrip on day to day basis resulted in fall in the price of the scrip. After executing their motive successfully, FGSB had covered their sales position.

6. In the scrip of Zee, the Enquiry Officer observed that in Settlement No.1046, the member had a net sale position of 195655 shares which constituted -7.60% to the exchange net. Out of the settlement, 4,5 & 10, where the member had buy deferral quantity, only settlement No.10 falls between 6<sup>th</sup> March to 13<sup>th</sup> March.

FGSB had stated that the Enquiry Officer acted with double standards as the alleged net sales in settlement 1046 (5/2 to 10/2) and then proceeded to disregard buys because one falls within mid February to mid March.

We have examined the contention of FGSB. We do not find that the Enquiry Officer acted with bias. The net sales in Zee Tele are quite high and we can not but come to a conclusion that the member is responsible for the depression of the scrip price.

7. In the scrip of Infosys, the Enquiry Officer observed that the carry forward sales of 1775 shares in Settlement no.1047 are small and insignificant. The member had a net carry forward sale of 15000 shares which was subsequently covered in Settlement 1049. He found that the trading pattern throughout did not indicate any bearish pattern.

The Enquiry Officer has exonerated FGSB on this count. However we are of this opinion that the totality of trading pattern should be seen and there is no question of weakening the theory of intention to manipulate the index levels.

8. In the scrip of Sterlite Optical, the Enquiry Officer observed that only one single position was maintained. There was very low trading indicating that there is no intention to deal in that scrip.

We have looked into the explanation of FGSB. We do not find any substance in the submissions. FGSB has already taken considerable (compared with the Exchange sale carried forward position) sale position in this scrip which was carried over to three settlements, which itself shows that the member had created sale pressure in this scrip.

9. With regard to cancellation of sale order, the Enquiry Officer concluded that this charge had not been established. However we are of the opinion that the relevant facts should be seen in totality and not in isolation.
10. On the analysis of trading by FGSB on 23<sup>rd</sup> February 2001. 1<sup>st</sup> & 2<sup>nd</sup> March 2001 at NSE & BSE, Only Settlement No. 7 to 10 covers the period between mid Feb & mid March. The net sales of the member were compared with the net sales at the exchange. It cannot be compared with the aggregate trading volumes which comprises of both sales and purchases and such comparison would give a distorted view. A consistent pattern of squaring off positions by purchases, if they are preceded by carry forward sales would give credence to the argument that the member is causing a fall in price market price of the shares to gain by purchases at reduced prices.
11. With regard to HFCL enquiry officer observed that they had a cumulative net sale position of 15000 shares on 19<sup>th</sup> February 2001 and cumulative buy position of 40000 shares on 17<sup>th</sup> February 2001. There is unwinding of long positions by the member.

We agree with the findings of enquiry officer.

12. We have taken note of other trading details and are of the view that the trading was on the similar lines at NSE.

#### **9.5 Whether FGSB and VCIP indulged in short sales to artificially depress the share prices.**

As observed by the enquiry officer the net sale position of the member has been compared with percentage net at the exchange. It cannot be compared with total volumes which comprises both purchases as well as sales. Any such comparison would give a distorted view.

The net sales during mid February and mid March was significant when compared with the net sales at the exchange. The net sales by the member cannot be compared with the trading volumes since it contains gross sales and purchases. Any such comparison would not lead to correct conclusions. Hence, taking into account the net sales by the member in the aforesaid instances, Enquiry Officer has concluded that such sales had resulted in artificially depressing the share prices in the aforesaid instances. The enquiry officer noted that it is not possible in such a situation, when there is substantial market fall, to determine with mathematical precision the amount of fall in share prices caused by a series of actions over a period of time by a market participant. Overall view of the market and the trading behaviour of the member under the circumstances during the relevant period has to be taken into account. In this connection, the carry forward sales by the member in BSE in the following scrips as a percentage of total carry forward in the exchange is also taken into

consideration in addition to the net sales by the member.

| Settlement no. | Scrip Name        | Sales carry forward at BSE | FGSB Sales Carried Forward | % of FGSB sales carry forward to exchange |
|----------------|-------------------|----------------------------|----------------------------|-------------------------------------------|
| 48             | Satyam Computers  | 508858                     | 85075                      | 16.72%                                    |
| 46             | SSI Ltd.          | 45283                      | 10596                      | 23.40%                                    |
| 47             | SSI Ltd.          | 78170                      | 50010                      | 63.98%                                    |
| 48             | SSI Ltd.          | 78569                      | 49000                      | 62.37%                                    |
| 49             | SSI Ltd.          | 142840                     | 54649                      | 38.26%                                    |
| 46             | Sterlite Opticals | 46296                      | 27489                      | 59.38%                                    |
| 47             | Sterlite Opticals | 40911                      | 25000                      | 61.11%                                    |
| 48             | Sterlite Opticals | 57179                      | 25000                      | 43.72%                                    |
| 47             | Wipro             | 161129                     | 15270                      | 9.48%                                     |
| 48             | Wipro             | 124133                     | 37783                      | 30.44%                                    |
| 49             | Wipro             | 131076                     | 50283                      | 38.36%                                    |
| 50             | Wipro             | 71016                      | 28300                      | 39.45%                                    |

The charges of short selling, carry forward sales, unwinding of previously long positions are examined in the light of the aforesaid arguments of the member. Allowance is given to the arbitrage positions and the other trades, where the member had significant buy positions and errors in the data as given in the enquiry report. The enquiry officer agreed that the member had not exceeded the carry forward sales limits of the exchanges. The percentage of carry forward sales of the member against the total carry forward sales at BSE is high in the relevant period in the scrips of Satyam, Software solutions, Sterlite Opticals and WIPRO. The Enquiry Officer observed that the short sale is a permitted activity but what is to be seen is whether the trading behaviour of the member between mid Feb and mid March in the select scrips has contributed to artificially depress the share prices. The enquiry officer found that the overall trading by the member during the aforesaid period has contributed for the fall in share prices."

After going through the reply of FGSB we do not find any reason to interfere with above findings of the Enquiry Officer.

## 9.6 Whether the sales during the specific time slots contributed to the fall in market.

We find that in the show cause notice, the instances of sales during the particular time slots when the scrip prices registered substantial fall has been given. FGSB and VCIP has contended that the show cause notice given on order placement during specific time slots but the data pertains to order execution.

With regard to order placement in specific time slots by FGSB, the Enquiry officer has found that in three transactions involving sale of shares by FGSB during specific time bands impacting the share prices, on the specific dates, instances involving the sale of Wipro at BSE on 23<sup>rd</sup> February, and 27<sup>th</sup> February, 2001, the short sale by the member during the specific time slots had caused the price fall.

As already stated the time slots were selected keeping in view the period of fall in the scrip. Though the member contended that the data pertains to order execution and not order placement, the member did not give any data on the timings of orders placed for the relevant executions. We therefore find that this is only a technical defect which the FGSB wanted to highlight with a view only to side track the issue. It is admitted fact that FGSB was present as a big seller almost every time there was a major fall in the scrip as proved above and it can be concluded that they are the main contributor for the depression of the market.

We concur with the Enquiry Officer that the charge was established to the extent of three transactions as stated above. This is in violation of Regulation 4(a) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to securities markets) Regulations, 1995.

## 9.7 Whether FGSB indulged in dealing with unregistered sub brokers:

9.7.1 With regard to charge that there was circular trading and routing proprietary trades through unregistered entities, Enquiry Officer found that the member had dealt with Palombe Securities which is an unregistered sub-broker. Enquiry Officer relied on the statement of Bhaskar Hingad dated 3.8.2001 who stated that Palombe Securities would be responsible for payment to Bang Equity in case of default. This is as it normally is between a broker and a sub-broker. Thus Palombe Securities is an unregistered sub-broker. The fees received by Palombe from Bang is more than mere introductory fees because he is also undertaking the liability in case of a client's default. Therefore, Enquiry

Officer concluded that FGSB was dealing in securities through an unregistered sub-broker which is unbecoming of a registered stock broker.

9.7.2 We find that the Enquiry Officer concluded that the Director of FGSB / member had dealt with Palombe Securities which is an unregistered sub-broker. We find that an amount of Rs.30 lakhs has been passed on to the Palombe Securities merely for introduction as finder's fee / introducing fee. It is also for consideration whether a person having its own broking firm will conduct proprietary trading in such a way which entail payment of an amount of Rs.60 lakhs as brokerage to other firms such as Nirmal Bang Securities. We also find that an amount of Rs.20 lakhs was received by FGSB from Palombe even though FGSB had denied any relationship with Palombe Securities. We agree with the findings of the Enquiry Officer that FGSB dealt with an unregistered sub-broker

#### **9.8 Whether there is a violation of SEBI ( Portfolio Managers ) Regulations,1993**

We find that one RNA builders which is primarily engaged in construction and real estate business had placed approximately Rs 20 crores at the disposal of FGSB, claiming for the purpose of arbitrage trading in the securities on its behalf with the object of earning profit in the arbitrage trading. We find that incase of normal arbitrage trading an arbitrageur places simultaneously buy and sell order in two exchanges and executes the order to get the price differentials. However, we find that in this case FGSB has been buying continuously at one exchange and thereafter (and not simultaneously) made sales at the other exchange. We find that decisions relating to the security , quantity and the time to purchase were left to the FGSB. Any loss arising out of such trading is absorbed by FGSB. Every week FGSB used to send statement to the RNA group containing date wise purchase and sale made by the FGSB along with the amount of investment. The said statement shows that the arrangements between the FGSB and RNA group was that the fund placed by RNA group at the disposal of FGSB were made to earn a minimum return. It is also found that FGSB could utilise the funds placed with them by RNA group for its own stock operations, on the condition that it would pay a definite return on disinvestment to RNA Group. The portfolio manager regulations prohibit return sharing , funds of the client to be kept in separate account, and cannot be utilised by broker/portfolio manager for its own purposes, portfolio manager cannot guarantee or paid assured returns and cannot indulge in speculative transactions while dealing with the clients funds. We find that FGSB and others have been carrying out portfolio operations under the guise of arbitrage trading and some of the operations as referred to above was in violation of Portfolio Managers Regulations. In this context the alleged mis-statement in Enquiry report with regard to absorbing of losses to Sauda Error is of no relevance.

#### **9.9 Whether FGSB indulged in Matched Trades /Synchronised trades in violation of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995 .**

The Enquiry Officer noticed that transactions between FGSB & Bang Equity were synchronized transactions in view of the close proximity of the order time punched by both the parties in the system. Both the firms had entered buy and sale orders for the same quantity of shares almost simultaneously. There is no transfer of title in these shares since the purchase and sale quantity are exactly the same. For the matched trades, the difference in time space is as little as just a second in the case of Sterlite for 1<sup>st</sup> March 2001 for 50,000 shares. While in some cases, there is 100% matching of the buy and sale quantity. In other cases, majority of the order quantity got matched. The more the gulf between the order timings, the less it is likely to get matched. The value of such transactions are also quite high. Such transactions are irregular and defeat the purpose of normal order-matching system in the price discovery process in the exchanges and would also be in violation of Regulation 4 ( c ) & (d) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to securities market) 1995."

FGSB has submitted that when the trading/exposure limits of FGSB and associates were exhausted or likely to be exhausted or when heavy constituent demand was expected , in such circumstances, certain trades or proprietary trades were shifted to the Bang Equity. It was further submitted that as and when limits were available with FGSB and associates such trades were generally shifted back to the FGSB. We find that in the electronic order entry system, as in vogue in India , the counter party is always anonymous. But the very fact that FGSB knew the counter party before executing the trade frustrates the screen based transparent trading. Such trades militates against transparency and do not contribute towards price discovery and therefore operates against the basic concepts of Stock Exchange. Thus, such shifting of position and synchronized trading interferes with functioning of Stock Exchange and price discovery mechanism which undermines the confidence of investors in the securities market.

#### **10. Whether FGSB indulged in Order cancellation which resulted in violation of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995**

We note that the FGSB has done order cancellations. It has been contended that it is a normal market practice to cancel an unexecuted order. We are of the opinion that cases where a person offers to sell large quantity of shares to impact the market and after the price comes down, cancels his previous order for sale, the same is irregular. Such practices are known as spoofing and are to be seriously viewed as the same interferes with the normal price discovery mechanism and induces other investors to trade on such orders which are subsequently cancelled.

#### **11. Whether Show cause notice dated 6<sup>th</sup> October ,2001 in in excess of the jurisdiction of the Enquiry Officer**

FGSB has contended that the show cause notice dated 06.10.2001 is bad as the Enquiry officer was not appointed to issue such show cause notice. We have perused the order dated 25<sup>th</sup> May, 2001 appointing the

Enquiry officer. We find that the Enquiry officer was appointed as such pending investigation. In the said order it was clearly mentioned that the Enquiry officer will conduct enquiry in respect of pending investigations and would issue notices as and when any portion of investigation is completed. The Enquiry officer issued the first show cause notice on 17<sup>th</sup> July, 2001. Soon after receipt of subsequent interim report the Enquiry officer forwarded further show cause notice dated 6<sup>th</sup> October, 2001 along with the copy of the relevant portion of the interim report. The show cause notice dated 6<sup>th</sup> October, 2001 was thus in continuation of earlier show cause notice dated 17<sup>th</sup> July, 2001. Therefore, we find that the show cause notice dated 6<sup>th</sup> October, 2001 was in accordance with order dated 25<sup>th</sup> May, 2001.

#### **9.12 Whether FGSB is guilty of Evasion of Margin**

With regard to charge that FGSB & VCIP evaded margins by showing proprietary trades as Institutional trades, the Enquiry Officer found that the charge relating to evasion of margins by FGSB and VCIP has been established.

We carefully looked into the issue. In regard to these transactions at NSE, It has been observed that FGSB vide its letter dated 12<sup>th</sup> July 2001 has admitted that due to trading pressure the dealer may have inadvertently marked these trades as FII trades.

FGSB in their reply submitted a chart containing net effect of such trades on gross exposure of the member. However FGSB had conveniently projected the data by ignoring intra day effect of such trades on the gross exposure. It is also observed that FGSB has executed certain trades in such a manner to circumvent objective of such trading restrictions and margin requirements.

We find that FGSB has evaded margin by showing non institutional trades as institutional trades at BSE and NSE. We find during the period from 1<sup>st</sup> October, 2000 to 1<sup>st</sup> January, 2001 the sum of margin evasion when there is no capital to meet margin amount is Rs 6.26 Crores and total margin evasion was 12.16 Crores on account of non institutional trades being shown as institutional trades at BSE. We further find that NSE vide its letter dated 2<sup>nd</sup> August, 2001 has confirmed imposition of fine on FGSB for evasion of margin and which has been paid by FGSB. Thus FGSB has been showing non institutional trades in order to avoid payment of margin. Such a conduct puts the risk management system of the exchange in jeopardy and is detrimental to the interest of the securities market.

#### **14. Whether FGSB violated SEBI circular dated 7<sup>th</sup> March, 2001 on short sales**

SEBI vide its circular dated 7<sup>th</sup> March 2001 restricted short sales. If at the time of execution of sale order, if the member does not have securities or corresponding buy position the same would be in violation of above circular. We find that M/s Vijay Mehta Chartered accountants of BSE had certified short sales on or after 8<sup>th</sup> March, 2001 done by FGSB. The said short sale was for an amount of Rs 10 crores.

FGSB has stated that the said transaction was on behalf of their clients and not their proprietary trades and also contented that the enquiry officer furnished floppies and diverse data which was all data in support of the charge during the hearing without any opportunity to crosscheck or verify the same.

We observed that, FGSB had raised this issue but not disputed the data given by the enquiry officer on 1<sup>st</sup> January 2002. As FGSB neither raised objection in the hearing before the Board nor filed written submissions disputing the above said data, there is no merit in their contention. We therefore find that the FGSB and VCIP executed the sales in contravention of SEBI Circular No. SMDRP/Policy/Circular-13/2001 dated 7<sup>th</sup> March 2001.

#### **15. Whether FGSB and VCIP are guilty of Non-Co-operation with Investigations in violation of SEBI Act, 1992.**

SEBI had sought certain information regarding the payments made by FGSB to its group /Clients, which were not submitted. Information sought relating to the trading transactions of First Global (Mauritius) were also not submitted and summons issued by SEBI under the Act for furnishing of the information were not complied with.

FGSB contended without admitting the above charge that for such non-cooperation the remedy is under 15A of SEBI Act.

The Enquiry Officer has concluded that FGSB has not cooperated in the on-going investigations and even summons issued for furnishing of information were not complied with. The Enquiry officer has concluded that the charge of non-cooperation with the regulatory body has been established. We do not find any material to interfere with this finding of the Enquiry Officer.

### **10.0 Conclusions**

1. From the above discussion we find that FGSB and VCIP had indulged in large trading transactions in the scrips of Global Telesystems, HFCL, DSQ Software, Zee Telefilms, Wipro, Satyam Computers, SSI and Sterlite Opticals with a view to artificially depress the prices of the above said scrips, which in turn was responsible for the market fall.

2. They adopted a pattern, which includes large carry forward sales, sales in above said scrips on specific dates, sales in particular time slots when the scrips prices registered substantial fall, portfolio operations disguised as structured arrangements in the garb of arbitrage trades, routing of proprietary trades through non-descript unregistered sub-broker. This establishes a concerted attempt to manipulate the prices of the scrips.
3. In the fact and circumstances of the case, the conduct of FGSB and VCIP is not in consonance with the high standards of integrity, fairness and professionalism expected from a Stock Broker and Portfolio Manager. They also failed to co-operate with the Board at various stages. We find that FGSB and VCIP are guilty of violating the code of conduct specified in Schedule II of the SEBI (Stock Brokers and sub-brokers ) Regulations, 1992, Regulation 4 (a) to (d) of SEBI (Prohibition of Fraudulent and Unfair trade practices relating to securities market ) Regulations, 1995 and Regulation 14 (3) of SEBI (Portfolio Managers ) Regulations, 1993.
4. In light of the above, we are of the considered view that FGSB and VCIP has indulged in manipulating the prices of scrips and depressing the market. They interfered with smooth functioning of the market and acted in a manner, which erodes the confidence of the investors and adversely affects the integrity and the healthy growth of the securities market. Therefore we agree with the penalty recommended by the Enquiry officer and we do not find any mitigating circumstances or reasons to reduce it to a lesser penalty.

#### **ORDER**

We, in pursuance of the directions of the Hon'ble High Court of Bombay and in exercise of the powers conferred by section 4(2) of SEBI Act, 1992 read with Regulation 13 of SEBI (Prohibition of Fraudulent and Unfair trade practices relating to securities market ) Regulations, 1995 read with Regulation 29(3) of SEBI (Stock Brokers and sub-brokers ) Regulations, 1992, and Regulation 35 (3) of SEBI (Portfolio Managers ) Regulations, 1993, hereby cancel the certificate of Registration granted to FGSB as Stock broker (SEBI Reg. No. INB230722136 and INB010722152) and Portfolio Manager (SEBI Reg. No. INP000000381) and VCIP ( SEBI Reg. No. INS010647738/01-07221) as a Sub-broker. This order shall come into effect immediately. However as per the directions of the Hon'ble High Court of Bombay vide its order dated 11<sup>th</sup> April 2002 in WP no. 824 of 2002 this order stands stayed for four weeks from receipt of the copy of this order by them. Till such time SEBI's order dated 25<sup>th</sup> May 2001 passed under section 11B of SEBI Act, 1992 shall remain operative against them as directed by the Hon'ble High Court of Bombay in its order as aforesaid.

**G. .N. BAJPAI V.K. DHALL G.P.MUNIAPPAN**

**Chairman Member Member**