

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER UNDER SECTION 11(4) OF SEBI ACT, 1992 AGAINST HARVEST DEAL SECURITIES LTD. IN THE MATTER OF NEDUNGADI BANK LTD.

CO/ /2003/IES/FUTP

1.0 SEBI had conducted investigations into the alleged violations of the provisions of SEBI Act, Rules and Regulations made there under, Securities Contract (Regulation) Act, 1956 as well as the Rules, Regulations and Byelaws of the Exchanges by Harvest Deal Securities Ltd. (herein after referred to as 'HDSL') along with its associate brokers namely First Custodian Fund India Ltd. (herein after referred to as 'FCFL') and Shrikant G. Mantri (herein after referred to as 'SGM') in its dealings with Nedungadi Bank Ltd. (herein after referred to as 'NBL') during the period September, 1999 to March, 2000.

2.0 Subsequent to the investigation, a show cause notice dated March 11, 2003 was issued by SEBI to HDSL asking them to show cause as to why directions under Section 11B of SEBI Act, 1992 read with Regulation 11 and 12 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995 should not be issued pending enquiry. HDSL was alleged to have indulged in the acts mentioned below :

- issued bogus contract notes;
- did not account for the contract notes which have been issued;
- delayed payments to the bank;
- entered into one sided transactions;
- made late delivery of securities; and
- did not obtain written agreement from the client,

which were in violation of regulation 6 (a), (c) and (d) of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices) Regulations, 1995. Through the above acts, HDSL was alleged to have violated clause A (1), (2) and (5) and clause B (1) of Schedule II of the Code of Conduct for Stock Brokers read with regulation 7 of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992.

3.0 A letter dated March 17, 2003 from HDSL was received by SEBI wherein they had stated that Mr. Rajendra Kumar Banthia, its director was out of Mumbai and would be back only by the last week of March and therefore they had asked for further date for inspection. In another letter dated March 19, 2003, HDSL requested for further time to file the reply after inspection of documents and also personal hearing before the Chairman. Thereafter, SEBI vide its letter dated March 26, 2003 duly granted inspection on March 27 and March 28, 2003, which letter was received by them on the same day. The opportunity for inspection was availed by HDSL on March 27, 2003. Accordingly, the documents were inspected by their representative, Mr. Prakash Shah, their Chartered Accountant. During inspection, the representative of HDSL had requested for copies of certain documents available with SEBI. The same were furnished to them vide letter no. IES/ID5/RM/7134/2003 dated April 09, 2003.

3.1 An opportunity of hearing was granted to HDSL on April 10, 2003 vide letter dated April 09, 2003. During the hearing, no one represented HDSL.

3.2 A letter dated March 10, 2003 in response to the show cause notice was received by SEBI on April 21, 2003. In the said letter it had been said that HDSL was an independent legal entity and not connected with SGM or FCFL in any manner as alleged in the show cause notice. It had said that the subject matter of HDSL, being a separate entity was before the High Court of Bombay in W.P. No. 2381 of 1998. Further, it was said that the contentions in the show cause notice with respect to its dealings with NBL is subject matter of W.P. No. 356 of 2003. HDSL had desired for further time of 15 days to file reply to the show cause notice. They also denied each and every allegation in the show cause notice. However, a letter dated May 12, 2003 was received by SEBI from HDSL stating that they have discontinued their business activity in February 2002 and vide letter dated November 18, 2002, the same has been informed to the Stock Exchange, Mumbai. They also submitted that consequent to the voluntary closure of business, the concerned directors were not in town and hence they were not in a position to reply to the show cause notice.

4.0 I have carefully considered the investigation report, findings and charges in the Notice, statements and other evidences available. As per the minutes of the NBL Board Meeting, HDSL, a member of BSE was found to have entered into arbitrage transactions on behalf of NBL during the period September, 1999 to March, 2000 with the approval of the NBL along with the following brokers :

1. M/s Shrikant G. Mantri (SGM) Member - BSE
2. The First Custodian Fund (India) Ltd (FCFL) Member - NSE

4.1 At the end of March, 2000, the trading in arbitrage deals was found to have been stopped by the NBL. It was observed that the trading transactions, which were part of the NBL's investment portfolio were carried out by HDSL along with its associates, FCFL and SGM. NBL's total turnover of trading with the above three brokers reportedly stood at Rs.1352.54 crores while transactions with the other approved brokers was insignificant at Rs. 0.26 crore which was mainly due to sale of shares from its investment portfolio. It was also found that there had been a default as well as delay in payment of the sale proceeds by the above brokers to the NBL. As a result, the dues from the brokers to the NBL were found to have stood at Rs.94.61crores as on 31st March, 2000. Though, out of this, an amount of Rs.73.42 crores was found to have been paid to the NBL over a period of one year, a sum of Rs.21.10 crores was found outstanding from SGM as on 31st March, 2001. The above firms were found to be owing an amount of Rs. 8.72 crores towards interest charged for the delayed payment of sale proceeds.

4.2 Shri. R. K. Banthia is found to have been the Managing Director of HDSL. He is also found to have been one of the directors of the NBL, having substantial shareholding, either directly or through his family members/associated firms / companies. Out of the total shareholding in NBL, the Rajendra Banthia Group held 8.41%, FCFL a Member of NSE and also an associate of Rajendra Banthia held 3.28%, and SGM, member BSE and also an associate of Rajendra Banthia held 10.51% of the equity of the NBL.

4.3 It was also found that over the period when the NBL decided to engage in arbitrage dealings i.e. vide the Board Meeting held on 26.06.99, Mr. M. G. Damani and Mr. Suresh G. Vaidya had represented Banthia Group on the Board of Directors of the NBL. In fact Shri M. G. Damani and Shri A. R. Murthy had suggested to the Board for engaging the services of HDSL, FCFL, and SGM. Subsequently, Mr. Rajendra Banthia was found to have been co-opted on the Board of the NBL on December 26, 2000.

4.4 Investigations had revealed that the three broking firms, FCFL, HDSL and SGM were closely connected to each other. Mr. Rajendra Banthia was found to be the Managing Director of the HDSL in which Smt. Saroj Banthia, Mr. Rajendra Banthia's wife and Shri. Manish Banthia, Mr. Rajendra Banthia's son were also Directors. In FCFL, Shri. Surendra Kumar Banthia, Mr. Rajendra Banthia's brother was the Chairman and Shri. Manish Banthia, Mr. Rajendra's son was the Director. Shri Sushil Mantri, Executive Director of this broking firm, was the brother of SGM. Thus all the three firms were to be closely associated with Shri. R. K. Banthia. All the three broking companies had functioned from the same premises and had common phone and fax connections which clearly indicated that these companies were closely connected. The purchases and sales were found to have been effected in different exchanges through these brokers' which further proves the common linkages of these brokers. The exact linkages are represented through a diagram given below:

Harvest Deal Securities

R.K. Banthia

(Managing Director)

Saroj Banthia (wife)

(Director)

Manish Banthia (son)

(Director)

First Custodian Fund (India)

Ltd.

Surendra Kumar Banthia

(brother of R.K. Banthia)

(Chairman)

Manish Banthia (son)

(Director)

Sushil Mantri

(brother of Shrikant Mantri)

Executive Director M/s Shrikant G. Mantri

Shrikant Mantri

(Proprietor)

4.5 The arbitrage transactions on behalf of NBL seem to have been done to capitalize the price differences existing in the NSE and BSE due to the different settlement cycles followed by them. Purchase and sale had to be executed simultaneously and put through with accuracy and great speed and so the Chairman and General Manager were to be permitted to delegate their powers to purchase/sales to the above three brokers. The purchase and sale were to be executed simultaneously in view of the risks associated with the unfavourable movement of prices of shares. To take care of other risks, trade had to be done as far as possible in shares of reputed companies and deals were to be carried out in the demat form.

4.6 However, before entering into the dealings with NBL, HDSL was found to have not obtained a client registration form and agreement duly filled in by NBL while taking them as their clients. This appears to be in violation of SEBI circular No. SMD/POLICY/CIRCULARS/5-97 dated April 11, 1997 and thus the brokers including HDSL appears to have violated Clause A(5) of Schedule II of the Code of Conduct for Stock Brokers read with Regulation 7 of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992.

4.7 The investigations had revealed HDSL and its associate brokers had a free hand in the buying and selling of scrips on behalf of NBL and had carried out transactions according to the discretion of HDSL. The details of the deals such as name of the scrip, purchase order, sale order, quantity, rate etc. was found to have been decided by HDSL and its associate brokers. Shri R. K. Banthia who was a major shareholder of the NBL was also a Director of the NBL during December, 2000 to April, 2001 and Managing Director of HDSL. He played a key role in buying and selling of the shares through his associate brokers. It was found that that Mr. Banthia had exercised undue pressure on the Chairman/Board of NBL for the purpose of purchase and sale of shares. During R. K. Banthia's tenure as a Director, the Board of the NBL was found to have decided in January, 2001 to make investment of Rs.30.00 crores in shares, convertible debentures etc. which further indicates his influence on the decisions of the NBL.

4.8 It was observed that SGM had overdraft limit of Rs.500 lakh and guarantee limit of Rs. 600 lakh each from NBL. FCFL, another associate broker of HDSL, also had an overdraft limit and a guarantee limit of Rs. 500 lakh from NBL. NBL was found to have entered into frequent and large purchase / sale transactions through HDSL and its associate brokers in various scrips. Most of the transactions were not executed as arbitrage transactions i.e. purchases / sales of equal quantity of the particular shares were not executed simultaneously through different exchanges. For example, NBL was found to have purchased 6500 shares of Lupin Laboratories on 26.11.99 through its associate, SGM, whereas the sale of 1500 shares was on 26.11.99 and the remaining 5000 shares were done on 29.11.99. Similarly it bought 2450 NIIT shares on 01.11.99 through its associate, FCFL and sold only 950 shares on 01.11.99 through SGM and the balance quantity was found to have been sold on the subsequent days i.e. on 2nd and 3rd November, 1999. NBL had bought 22400 shares of Silverline on 09.11.99 which were sold to the extent 12400 shares on 09.11.99 and the balance 10000 shares were sold on 10.11.99. There had been several transactions of the above nature. Therefore, these transactions were not of arbitrage dealings and had been open positions/investments of short term nature.

4.9 From the details of transactions in the demat accounts, frequent inflow and outflow of shares with HDSL and its associate brokers were observed. Similarly frequent inflow and outflow of funds with the brokers were also observed towards the purchases and sales of shares. This indicates that the NBL was taking positions in various scrips through HDSL and its associate brokers instead of pure arbitrage transactions.

4.10 Investigations had revealed that during the last week of March, 2000 the sale transactions of NBL through its associate, SGM was to the extent of Rs. 58.7 crores. There had been dealings mainly in the scrips of infotech companies like Pentafour Software, Global Telesystems, Himachal Futuristic, Moser Baer and DSQ Software. Other scrips included ACC and Zee. These transactions were of the nature of off market deals and were not done through the exchanges. The above deals were all one sided transactions in the sense that there was no purchaser for the above scrips which were reportedly sold by the NBL through its associate, SGM. All the prices at which the above scrips were shown to have been sold were significantly above the then market prices prevailing at that point of time. For example, Pentafour Software share price on 27.03.2000 was Rs.1311.50 on BSE and Rs.1356.53 whereas the sale price of the bank on the date was reported to be Rs.1807.65. Similarly, HFCL's sale price was Rs.2140.10 on the BSE and Rs.2147.20 on NSE whereas the reported sale price was Rs.2200. There were other scrips too which were sold in huge quantities and had similar discrepancies in the prices. The major discrepancies in the above sales transactions are as follows:-

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No deliveries were obtained from the NBL for the above sales by the brokers.

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There were no payments from the brokers to the NBL for the above deals.

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The brokers had issued contract notes for the above transactions but had not accounted for the transactions in their books of accounts.

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However the NBL had accounted for the above deals in their books of accounts for the year ending March, 2000 based on the above bogus contract notes.

4.11 Investigations had revealed that the above referred transactions were bogus transactions. The contract notes did not have the time of transaction and also the same had not been entered through the exchange. The reason for issuing such contract notes seems to be accommodating NBL to hide its losses. The NBL had huge outstanding investment in the share market and the market had started falling after the purchases. The prices of the scrips in which the NBL had open position had fallen to a great extent. The NBL had to close its book of accounts for the year and it was be showing huge losses because of the above reasons. HDSL along with its associate brokers was found to have entered into a clandestine arrangement with NBL whereby the broker would issue bogus contract notes only for the purpose of accommodation and not for the purpose of acting upon it. In this regard, it was observed that, Rajendra Banthia, Managing Director of HDSL had acted as the main persons in coordinating the deals.

4.12 On the basis of the Contract notes furnished by its associate, SGM during investigations, it was found that he had sold 25,000 Himachal Futuristic shares on behalf of NBL on 23/08/2000, 70,000 shares on 24/08/2000 and 86,159 shares on 25/08/2000 with an aggregate sale price of Rs. 27.29 crores and an entry was made in the books of accounts of SGM. Again 3000 shares of the same scrip were found to have been sold on 29/08/2000 and 18439 shares on 31/08/2000 the entries for which were made in the books of accounts of SGM on 07/09/2000. But corresponding entries are not found in the books of accounts of the NBL. However, as stated earlier during March 2000, NBL was found to have transferred the shares to the brokers towards sale transactions. The entries made in the books of accounts of the broker for the month of September with respect to the same is bogus which proves nexus between the brokers and the NBL for their mutual accommodation by way of fictitious deals.

4.13 During the investigations it was observed that during March, 2001 HDSL's associate, SGM had purchased 50,000 shares of Jindal Steel, 400000 shares of Saw Pipes aggregating to a value of Rs.5.50 crore on 14.03.2001 for NBL. On the same day, another associate FCFL was found to have contracted for the purchase of 176500 shares of Monnet Ispah and 29500 shares of Ranbaxy Labs aggregating to Rs.5.04 crore on behalf of NBL. However, the investigations had revealed that NBL had not agreed to these transactions as they had not placed any orders with HDSL and its associates and that they had thrust the transactions on them. It was found out that Mr. Banthia had insisted on NBL to make payment for these purchases although NBL had not accepted on these contracts. This clearly indicates that Shri Rajendra Banthia was instrumental in influencing NBL for entering into these bogus transactions. Further these deals were not effected through the exchange and were off market deals. It appears that the said transactions were for the purpose of accommodation and not for the purpose of acting upon. On examination of the statements of the associate brokers of HDSL, it was observed that these brokers had these stocks in their portfolio which they had offloaded to NBL in order to mobilize funds. All these reiterates the nexus between NBL and the brokers for the purpose of hiding the factual positions.

4.14 The investigations also revealed that HDSL and its associates had delayed payments to NBL the details of which are given below:-

HDSL was found to have owed a sum of Rs.16,24,00,996 towards sale of shares on 06.03.2000 and Rs.3,58,44,527 towards sale on 07.03.2000 which he had failed to pay in time to NBL. This amount was found to have been paid in installments from 13.06.2000 to 22.06.2000 i.e. after a delay of three months. NBL is reported to have claimed interest for the late payment which has not yet been settled by the broker.

SGM was found to have owed a sum of Rs.67,79,00,480 towards sale of shares by NBL during 06.03.2002 to 27.03.2000 which he had failed to pay in time to NBL. Out of this Rs.7.07 crores was paid on 16th and 17th May 2000 and Rs.40.00 crores was paid only in September, 2000 i.e. after a delay of about six months. As on 31.03.2001 an amount of Rs.21.19 crores was found due by SGM to NBL. After considering the interest on this amount (as submitted by NBL) a sum of Rs.35.51 crores was due from SGM to NBL.

FCFL was also found to have resorted to making delayed payments to NBL. For example, in Settlement No. 2000001, FCFL was found to have paid Rs.1.58 crores after a delay of 23 days and in Settlement no. 2000007, it paid Rs.1.56 crores after a delay of 16 days etc.

4.15 Thus HDSL and its associates seem to have withheld the payments due to NBL for considerable period of time and thereby delayed the payments to the clients. SGM was found to have owed an amount of Rs.21.19 crores to NBL as on 31.03.2001 besides the claim of interest for the late payment. These dues have basically arisen due to the disputed contracts (NBL recognizes the contracts whereas the broker claims that these are bogus) for sale transactions in March, 2000, for which contract notes had been issued by Shrikant G. Mantri during August whereas the entries for the same are not made in the books of accounts of NBL (the contract notes issued were bogus in order to accommodate NBL).

4.16 These delays in payment by HDSL and its associate brokers to their clients are in violation of SEBI Circular SMD/SED/CIR/93/23321 dated November 18, 1993. The brokers have also violated clause A (1), (2) and (5) and clause B (1) of Schedule II of the Code of Conduct for Stock Brokers read with regulation 7 of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992.

4.17 During investigations it was observed that there were some instances of delay in delivery of securities by HDSL and its associates to NBL towards their purchases as follows. For example in case of ACC, the scrip was purchased on 16.02.2000 and 17.02.2000 but the delivery was made on 20.05.2000 i.e. after a gap of almost three months. Similarly the scrip of HFCL was purchased on 06.03.2000 but the delivery was made in installments by SGM on 31.05.2000, 02.06.2000 and 13.06.2000 while a part of it was found to have not been delivered at all. In the case of Videocon International, the scrip was sold on 04.02.2000 and the delivery was made on 20.05.2000 and 31.05.2000. Similar delays were observed in other scrips like Jayant Agro, Kale Consultants and Hindustan Sanitary. During investigations, differences in the statement of accounts of the transactions of the NBL and the brokers' accounts were also observed.

4.18 In this process, HDSL along with its associated brokers namely SGM and FCFL had indulged in the following acts:

- issued bogus contract notes;
- did not account for the contract notes which have been issued;
- delayed payments to the NBL;
- entered into one sided transactions;
- made late delivery of securities; and
- did not obtain written agreement from the client,

Thus HDSL appears to have violated regulation 6 (a), (c) and (d) of the SEBI FUTP (Prohibition of Fraudulent and Unfair Trade Practices) Regulations, 1995. HDSL seems to have thus violated clause A (1), (2) and (5) and clause B (1) of Schedule II of the Code of Conduct for Stock Brokers read with regulation 7 of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992.

4.19 An enquiry officer has been appointed against HDSL to enquire into the above alleged violations and the enquiry is in progress. Meanwhile, keeping in view the gravity of the violations and prima facie case, preventive action is warranted in order to refrain / restrain HDSL from dealing in securities so that no further harm or detriment is caused to the securities market and that investors are not adversely affected.

5.0 In view of the above, HDSL and its directors, Mr. Rajendra Kumar Banthia, Mrs. Saroj Banthia and Mr. Manish Banthia are directed in the interest of investors and Securities Market under Section 11(4) of SEBI Act, 1992 not to deal in securities in any manner till further orders.

This order shall come into force with immediate effect.

G.N. BAJPAI
CHAIRMAN
SECURITIES AND EXCHANGE BOARD OF INDIA

Date : July 14, 2003
Place : Mumbai