

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER UNDER REGULATION 13(4) OF THE SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002 READ WITH SECTION 11 OF THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992, AGAINST M/S. M.J.PATEL SHARE AND STOCK BROKERS LTD., MEMBER - THE STOCK EXCHANGE, MUMBAI (BSE) IN THE MATTER OF M/S. SNOWCEM INDIA LIMITED.

WTMN/203/IVD/8/04

1.0 BACKGROUND OF THE CASE

- 1.1 M/s. M. J. Patel Share and Stock Brokers Ltd. (hereinafter referred to as `MJP' ) is a member of The Stock Exchange, Mumbai (hereinafter referred to as `BSE') and registered with Securities and Exchange Board of India (hereinafter referred to as SEBI) vide SEBI Registration No. INB 010989233.
- 1.2 The National Stock Exchange (hereinafter referred to as NSE) conducted an investigation into the dealings in the scrip of M/s. Snowcem India Ltd. (hereinafter referred to as SIL) for the period June 3,1999 to August 10,1999 and submitted their report to the Securities and Exchange Board of India (SEBI).
- 1.3 It was observed in the investigation report that the scrip of SIL recorded a dramatic increase in the average number of trades from 3 a day during the period March 1, 1999 to May 25, 1999, to as high as 173 a day during the period June 3, 1999 to August 10,1999. There was a major spurt in the total volume in the scrip. From an average daily volume of 12,521 shares during the period March 1, 1999 to May 25, 1999, it recorded a five-fold increase to 68,370 shares a day during the investigation period. The increasing trend in volumes was accompanied by the price rise in the scrip as well. The scrip price of SIL fluctuated between Rs.48.10 and Rs.55.80 during the period March 1, 1999 to May 25, 1999. From June 3, 1999, it started rising and touched Rs.127.95 on August 10, 1999. From the analysis of the trading details of various members along with their clients, NSE observed that some entities associated / close to the Snowcem Group had been actively involved in trading of its shares during the said period resulting in unusual spurt in prices and traded volumes. It was further observed that in some settlements their contribution was as high as over 90% of the total market activity.
- 1.4 Pursuant to the above, SEBI conducted investigation into the dealings in the scrip of SIL and observed that Kosha Investments Ltd.(KIL) was the predominant trader in the scrip during the aforesaid period of investigations. It was further observed that SIL had reissued forfeited shares which were allotted to one Shri Sourabh Ramrakh R Bora, one of the top clients, who had traded in the scrip. The money received by KIL from SIL was time and again utilized for the purpose of making payments to brokers. It was observed that the timing of the fund transfers from the books of the company to the account of KIL and from KIL to the accounts of the brokers/sub-brokers indicated the intentions of the company to manipulate the price of the scrip of SIL. On almost all the occasions, it was observed that the funds were transferred from the account of SIL and credited into the account of KIL prior to their placement of transactions in the scrip of SIL. KIL was identified as the promoter group company of SIL and this had been admitted by the management of SIL. It was further observed that KIL being the predominant buyer in the scrip, was responsible for the price movement in the scrip of SIL. From the trading details submitted by the exchanges, it was revealed to SEBI that KIL had employed manipulative tactics either to maintain the scrip price and / or to increase the price drastically. It was further observed that transfer of funds occurred frequently and that the management of SIL was directly responsible for the price movement in the scrip during the said investigation period. SIL transferred the funds to the account of KIL, its promoter group company, and on the very same day KIL transferred the funds to Shri Sourabh H. Bora to enable him to make payments towards the allotment of forfeited shares and Shri Sourabh Bora made payments to SIL in respect of the forfeited shares allotted to him. It was also revealed during the investigation by SEBI with regard to the fund transfers that SIL was well aware of the lending of money for the purpose of making payments towards forfeited shares. It was further revealed that Shri Sourabh Bora had given cheques during the first week of September,1999 and these cheques were presented to the bank for realization only in the last week of September,1999 and the actual realization of the cheque took place on October 1,1999 after the bank account of Shri Sourabh Bora was adequately funded by way of transfer of funds from SIL. In addition to the above observations during investigations by SEBI, the records indicated that Shri Sourbh Bora still owed more than Rs.6 crores to KIL which in turn owed more than Rs.15 crores to SIL which revealed that Shri Bora had not made the payments to the company towards the forfeited shares allotted to him and the whole matter was just a book entry and the company managed to create shares without actual infusion of funds. Subsequently, it was revealed in investigation that KIL and Shri Sourabh Bora indulged in trading in the scrip of SIL through MJP, a corporate member of The Stock Exchange, Mumbai, which was mainly catering to institutional and corporate clientele, besides a few retail clients who traded in the scrip of SIL on behalf of KIL and Shri Sourabh Bora. It was observed during investigation that MJP traded on behalf of KIL and Shri Sourabh Bora who were directly associated with SIL. Both these entities were acting hand-in-glove with the management of SIL. The records submitted by KIL to the investigating team pertaining to the details of amount advanced by them to other parties during the period March,1999 to December,1999 indicated that KIL had advanced an amount of Rs.1,16,62,500 to Shri M.J.Patel, Director of MJP during the aforesaid investigation period, which indicated connections of the MJP with KIL. It was further revealed in the Order Log analysis that the member had placed big orders for KIL and Shri Sourabh Bora when the average trading volume in the scrip was hovering around 40,000 shares a day. In view of the above observations and the role of MJP, it was revealed by

investigation that MJP violated SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 1995 and SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992.

2.0 ENQUIRY REPORT AND RECOMMENDATIONS OF ENQUIRY OFFICER

2.1 An Enquiry officer was appointed vide Order dated 10th July, 2002 for conducting enquiry into the affairs of MJP, member of The Stock Exchange, Mumbai (BSE), vis-a-vis his dealings in the scrip of SIL and possible violation of the provisions of the following :-

- (a) Securities and Exchange Board of India (Stock Brokers and Sub Brokers) Regulations, 1992; and
- (b) Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995.

2.2 The Enquiry Officer, after conducting the enquiry as per the procedure laid

down under the (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as "Enquiry Regulations") submitted a report dated March 4, 2004. The Enquiry Officer in its said Report recommended a major penalty of suspending the certificate of registration for a period of 4 months.

3.0 Issue of Show Cause Notice, Reply and Hearing

3.1 A notice dated 8th March, 2004 was issued to MJP asking it to show cause why action under the provisions of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 should not be initiated against them in violation of Regulation 4 of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to securities market) Regulations, 1995 and also in violation of the provisions of the Code of Conduct prescribed for stock brokers contained in Schedule II read with Regulation 7 of the SEBI (Stock Brokers & Sub Brokers) Regulations, 1992. MJP was directed to reply to the said notice within 15 days from the date of receipt of the notice.

3.2 In response to the notice, a reply was filed by MJP vide its letter dtd. 2nd April, 2004 and made the following submissions :-

- The enquiry process itself was not valid as the service of notice was not done as per the SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 in as much as the same was served directly and not through the Stock Exchange.
- The Enquiry Officer has not justified the recommendations for imposition of major penalty.
- The Enquiry Officer failed to restrict himself to the period of investigation i.e. June, 1999 to August, 1999 and he covered the period prior to and after the period of investigation.
- Their trades for purchases are in between the price range of Rs.52.25 to Rs.59.75 during the period of investigation i.e. 3rd June, 1999 to 10th August, 1999. Beyond that no purchase was done by them. They cannot be held responsible for the increase in the price of the scrip from Rs.50.00 on 03rd June, 1999 to 127.95 on 10th August, 1999.
- *The variation in price range from Rs.52.25 to 59.25 for buy trades executed by them on behalf of their clients was too insignificant to hold them responsible for aiding and abetting the price rise from Rs.50/- on 3rd June, 1999 to Rs.127.95 on 10th August, 1999.
- Their share in total number of trading days and total number of shares traded on BSE and NSE was very meager.
- The trades done by them after 5th July, 1999 but during the period of enquiry were for sale except one.
- Margins were not collected separately and specifically in as much as their clients had credit balances with them. The shares were delivered to them immediately in case of sale which did not require collection of upfront margin.
- Both KIL and Sourabh Ramrakh R Bora were their registered clients doing business for long. The Enquiry Officer has failed to establish / quantify the loss or damage caused to any single investor. The Enquiry Officer has failed to prove that the trades executed by MJP had induced any single investor to trade in the scrip of SIL.
- All the trades done by them had resulted into delivery whether given / taken and the corresponding payment whether paid / received and such trades show that none of them were either fictitious or to merely increase the volume.
- The trades in the scrip of SIL executed by them on behalf of KIL and Sourabh Bora were during 1999-2000 and submitted that they had not done a single trade either in SIL or in any other scrip for both the parties after MJP came to know that Sourabh Bora and KIL having been restrained by SEBI from buying, selling or dealing in securities for the stated period.

- M J Patel had loan/deposit of approx.70 lacs from M/s. Kosha Investments Ltd. for past several years. When the business was corporatised, the said amount of deposit was transferred to the company's (MJP) books. Out of the deposit of Rs.68.90 lacs, MJP had "repaid" Rs.55.50 lacs during 1998-90 leaving credit balance of Rs.13.90 lacs on 31/3/1999. Kosha Investment had "repaid" to MJP the amount of Rs.65 lacs during 2/9/1999 to 6/9/1999 totalling to Rs.78.90 lacs. Shri Patel was individually to receive Rs.26.87 lacs from Kosha Investment Ltd. as on 1/4/1999. He received Rs.51,62,500/- from the period 10/9/1999 to 29/11/1999 and stated that the amount payable to Kosha as on 31/3/2000 by Mr.Patel was Rs.24.75 lacs. While the period of investigation is June,1999 to August,1999, the loan/advance given/received, repayment received from Kosha Investment during the course of regular business was in the month of September to November,1999 which showed that the amount received in subsequent period had no connection whatsoever for acquisition of shares of SIL. The loans / advances received aggregating to Rs.1,16,62,500/- were not at all utilized for the purpose of purchase of scrip of SIL and that the same had been used for normal business activities. The break up of the loans and advances received and repaid to Kosha was submitted.
- MJP had placed order on behalf of clients as per their instructions and at the price indicated by them. Both Mr. Sourabh Bora and KIL had dealt with MJP in big quantity in many other scrips like Advent Computer, Bank of India, Datasoft App., Dr.Reddy Lab., DSQ Software, Global Tele, HCL Infosys, Asian Paints, Camlin,etc. KIL and Mr.Sourabh Bora being high networth clients for them, the quantity ordered by Mr.Bora and KIL was not at all high. The price indicated by the clients while placing orders were around prevailing market price, and not at a price exorbitantly higher / lower than the previous closing price. As a broker, MJP could not know about clients intentions and denied the allegations of having failed to exercise due skill, care and diligence in their dealings with the clients.
- MJP had not entered into / taken part, entered directly or indirectly in any transactions in the scrip of SIL with the intention of artificially raising or depressing the prices and thereby inducing the sale or purchase of securities by any person. Their trades in the scrip of SIL were fully backed by payment and delivery and, therefore, such trades cannot be called to have been entered into with a intention of not transferring beneficial ownership but to operate only as a device to inflate, depress, or cause fluctuations in the market price of the scrip.
- MJP have maintained high standards of integrity, promptitude and fairness in the conduct of all their business, as a stock broker.
- MJP has not indulged in any kind of manipulative, fraudulent and deceptive transaction and further denied having abetted the carrying out of transactions which are fraudulent and deceptive and that they disturbed the market equilibrium and harmed the interest of the investors.
- MJP denied the charge of non collection of margins from the clients and stated that they had complied with the margin stipulations and collected margins from their clients.

4.0 **SUBMISSIONS MADE DURING THE HEARING**

- 4.1 An opportunity of personal hearing was granted to MJP on 28th May,2004 and was attended by Mr. B.L.Sarda, representative of MJP. MJP was further granted hearing on 28th May,2004. Shri B.L.Sarda, Chartered Accountant, Shri S.C.Mantri, Chartered Accountant, Shri Mehul Patel, Director and Shri R.C.Gaur, Accountant represented MJP and submitted documents in defence of their case. MJP during the hearing made submissions that they had no linkage with the share dealings of SIL. MJP further submitted that the funds transactions they entered into with KIL was not a share transaction but a loan transaction which had no connection with share trading. MJP denied that there was any margin evasion on their part. They further submitted that they had not entered into any new transaction and pleaded that the suspension would cause irreparable damage to the investors / clients.

5.0 **CONSIDERATION OF ISSUES AND FINDINGS**

- 5.1 I have carefully considered the material available on record, the submissions made by M/s. M.J.Patel Share & Stock Brokers Ltd. vide his letter dated 6th December,2003 and 2nd April,2004 and its submissions made during the personal hearing dtd.28th May,2004. My findings are as follows:-
- 5.2 As regards the contention of the broker that the notice had not been served through the Stock Exchange, I find that the provision envisaging service of the notice through the SE is only an enabling clause, which does not vitiate validity of the notice otherwise served.
- 5.3 I observe that section 15 J of the SEBI Act 1992 enumerates the factors to be taken into account by the Adjudicating Officer while determining the quantum of monetary penalty. The enquiry proceedings carried out against MJP was under the provisions of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty Regulations, 2002). Regulation 13 of the Enquiry Regulations deal with recommendations of penalties to be imposed in non monetary terms. The Enquiry Officer has made his recommendations based on the findings of the Enquiry.
- 5.4 It had been observed during the investigations that there was hardly any liquidity in the scrip June 21, 1999. The comparison shows that for the three months period of March April and May 1999, the average trades were three a day. However, from June onwards the trading activity increased in the scrip and for the period June to August 1999, the density of trades increased to 173 trades per day.

- 5.5 I also observe that that while the three months of March, April and May 1999 recorded an average daily volume of 12,521 shares, the same spurted during the subsequent period to register a five fold increase to 68,370 shares.
- 5.6 I also note that as per the findings of the investigation, the price started rising from June 1999, price gained an impetus in June and rose to high in August 1999.
- 5.7 The scrip which was illiquid during the earlier months, started gaining in price and volumes obviously due to the activities of KIL and SHB. Investigations have brought out that KIL and SHB were entities close to the SIL group and their contribution in some settlements was as high as 90% of the total market activity.
- 5.8 I observe that MJP started buying for its client from June 21, 1999, when the price was Rs 52 and the purchases upto July 26, 1999 were made at an average acquisition cost of Rs 53.5 and sold shares during the later half of July when the price had risen substantially.
- 5.9 Following is table giving MJP's contribution to the total market activities for his clients:-

Date of the transaction	Name of the client	No of shares buy/sell MJP	Shares traded in market	% of the contribution to shares traded in market.
21-Jun-99	KIL	1,00,000	1,32,700	75.36
1-Jul-99	KIL	1,00,000	1,17,600	85.03
5-Jul-99	KIL	50,000	1,60,600	31.13
15-Jul-99	KIL	-1,25,000	1,32,100	94.63
19-Jul-99	KIL	47,900	1,58,700	30.18
23-Jul-99	SHB	1,00,000	1,15,600	86.51
26-Jul-99	KIL	-400	61,300	0.65

- 5.10 The above table indicates the concentration of the transactions of MJP w.r.t. to the total traded quantity. There had been hardly any trading activity prior to this period. The large purchases of MJP for its clients have resulted in creating an impression in the minds of the investors and have caused the rise in the price of the scrip.
- 5.11 The arguments that the trades done by MJP after July 05 1999 were for sale is misleading in as much as the sale represents a part of the purchases made earlier in the later half of June 1999 upto July 05, 1999.
- 5.12 The broker's submission that the then applicable percentage of upfront margin collection was 10% is incorrect. SEBI circular dated November 18, 1993 mandates the broker to collect from its client 20% margin for both the sale and the purchase transaction.
- 5.13 I note that the broker had not submitted, as claimed, the extract of the ledger account of his market transactions. The copies of the ledger documents that the broker submitted pertains to the loan account from KIL. Further, the statement depicting the dates of the transactions and the credit shown to have been lying with MJP is erroneous and the shares which were infact sold are found to have been shown as purchases.
- 5.14 I also note that these transactions had taken place in a weekly account period settlement cycle regime. I understand that the margins collected from the clients for their transactions were required to be utilized for satisfying their pay-in obligations and were not available for taking any further positions in the subsequent settlement till pay-out of the earlier settlement.
- 5.15 While the broker in his submission has given a reference to a circular dated December 04, 1998, I find that this circular only mandates that in case the margin liability of the client exceeds Rs 50,000/- then the brokers are required to collect this margin necessarily from the client and keep in a separate client account which shall then be used for meeting the settlement obligations on behalf of the client. At the time of these transactions with the clients KIL & SHB of MJP, the position w.r.t. margins was that MJP was supposed to collect 20% upfront margin from the clients with a threshold of Rs 50,000/- Keeping this in mind the aspect of short collection of the margins with respect to the purchase transactions of KIL is amply demonstrated in the following table:-

Sr no	Date of transaction	No of shares purchased	Value in Rs lakhs	20% Upfront margins to be collected	Margins available with the broker - recalculated	Margin shortfall
1	21-Jun-99	10,00,000	52.23	10.446	9.28	-1.166
2	1-Jul-99	10,00,000	51.26	10.252	-1.166	-11.418
3	5-Jul-99	50,000	29.88	5.976	<u>9.22</u>	3.244
4	19-Jul-99	47,900	25.58	5.116	<u>79.26</u>	74.144

- 5.16 From the above I note that the broker has failed to collect the stipulated margins at least on two days. MJP has also failed to satisfy that this margin was kept separately as margin money as required.

- 5.17 As regards the sale transactions the broker has argued that for these transactions the margins was not required to be collected as delivery of the shares sold were received on the very same day of the transactions. However, I find that this is not in compliance with the margin stipulations prevalent at that time, when it was mandatory to collect the shares before the transaction for the client was entered into. There fore I do not find any merit in the argument of MJP that margins are not required to be collected in case of sale transactions.
- 5.18 As regards the contention of the MJP about the funds flow from the KIL it is to be stated that this only establishes a relationship which is more than just a client broker relationship and that the MJP was aware that the KIL was a promoter group company of the SIL and should have exercised due diligence in the conduct of his business with respect to the heavy purchase made by the KIL during June 1999. This combined with the fact that the scrip was illiquid should have raised a note of caution for the broker. The submissions of the broker indicate his long standing relationship with the client KIL. From the trading details submitted by the broker I find that the two clients KIL and SHB aggregated 5,23,300 shares on a gross basis out of which KIL contributed to 80% of the trading done by MJP in the scrip.
- 5.19 I understand that KIL is a promoter group entity of the company SIL. I also observe that KIL has been restrained from buying, selling, or dealing in securities in any manner, directly or indirectly for a period of two years, vide order dated December 03, 2003. I also observe that vide an earlier order dated November 21, 2003 Saurabh H Bora was restrained from buying, selling or dealing in securities in any manner, directly or indirectly for a period of eighteen months. I find that MJP has dealt with transactions for both these clients.
- 5.20 I find that KIL and Shri Bora indulged in trading in the scrip of SIL, through various members of BSE and NSE, as mentioned in the table given below, which includes MJP:-

MEMBER NAME	EXCHANGE	MEMBER NAME	EXCHANGE
Indraprastha Holdings Ltd.	NSE	M.J.Patel Share & Stock Brokers Ltd.	BSE
Triveni Management Consultancy Services Ltd.	NSE	Bishwanath M. jhunjhunwala	BSE
Master Capital Services Ltd.	NSE	Kaynet Capital Ltd.	BSE
Kasat Sec.(P) Ltd.	NSE	NVS Brokerage (P) Ltd.	BSE

MEMBER NAME	EXCHANGE	MEMBER NAME	EXCHANGE
Nariman Finvest (P) Ltd.	NSE	Joindre Capital Services Sovereign Sec.(P) Ltd.	BSE

- 5.21 Regulation 7 of the SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992 provides that the stock broker holding the certificate shall at all times abide by the Code of Conduct as specified in Schedule II. Further, Clause A(5) of Schedule II provides that a stock broker shall abide by all the provisions of the Act and the Rules, Regulations issued by the Government, the Board and the Stock Exchange from time to time as may be applicable to him.
- 5.22 I find that MJP did not collect margin in compliance with SEBI Circular No. SMD/SED/CIR/93/23321 dated November 18, 1993 and Circular No. SMDRP/POLICY/CIR-35/98 dated December 04, 1998 and thus violated Clause A(5) of the Code of Conduct as specified in Schedule II of Regulation 7 of SEBI (Stock Broker and Sub-Brokers) Regulation, 1992.
- 5.23 Given the trading strategy adopted by the clients and the role of MJP, I conclude that MJP has aided and abetted his clients in price manipulation by executing orders on their behalf thereby violating the provisions of Regulation 4(a) &(b) of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market), Regulations, 1995. The Regulation 4(a) and (b) reads as follows :-

"4. Prohibition against market manipulation - No person shall-

- (a) effect, take part in, or enter into, either directly or indirectly, transactions in securities, with the intention of artificially raising or depressing the prices of securities and thereby inducing the sale or purchase of securities by any person ; and
- (b) indulge in any act, which is calculated to create a false or misleading appearance of trading on the securities market. "

- 5.24 I further note that Regulation 13 of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 reads as under :-

"Repeal and savings

13.(1) *The Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995 is hereby repealed.*

- i) *Notwithstanding the repeal of the Securities and Exchange Board of India ((Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995, any violation of regulations 3, 4, 5 and 6 of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995 shall be investigated and proceeded against in accordance with the procedure laid down in these regulations.*
- ii) *Notwithstanding the repeal of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995, any investigation pending, at the commencement of these regulations shall be continued and disposed of in accordance with the procedure laid down in these regulations."*

5.25 It is to be noted that persons who operate in the market, are required to maintain high standards of integrity, promptitude and fairness in the conduct of the business dealings. People, who indulge in manipulative, fraudulent and deceptive transactions, or abet the carrying out of such transactions, disturb the market equilibrium and harm the interest of the investors. Therefore, I, agree with the recommendations of the Enquiry Officer.

6.0 **ORDER**

In view of the foregoing, I, in exercise of the powers conferred upon me by virtue of Section 19 of the Securities and Exchange Board of India Act, 1992 read with regulation 13(4) and 13(6) of the SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002, and read with Regulation 12 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to securities market) Regulations, 2003, hereby direct that the Certificate of Registration granted to M/s. M.J.Patel Share & Stock Brokers Ltd., a member of The Stock Exchange, Mumbai, SEBI INB.010989233 be suspended for a period of four months.

This order shall come into force on the expiry of three weeks from the date of this order.

T.M.NAGARAJAN

MEMBER

SECURITIES AND EXCHANGE BOARD OF INDIA

DATE : 31ST AUGUST,2004

PLACE : MUMBAI