

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

UNDER REGULATION 13 (4) OF SECURITIES AND EXCHANGE BOARD OF INDIA (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002.

AGAINST ACME SHARES & STOCKS PVT LTD, MEMBER, THE STOCK EXCHANGE, BOMBAY, IN THE MATTER OF SAWACA BUSINESS MACHINES LTD. (EARLIER KNOWN AS SAWACA FINANCE LTD)

BACKGROUND

1. The shares of Sawaca Business Machines Ltd (earlier known as 'Sawaca Finance Ltd' and hereinafter referred to as 'SFL') were listed on The Stock Exchange, Bombay (hereinafter referred to as 'BSE') and Ahmedabad Stock Exchange.
2. Securities and Exchange Board of India (hereinafter referred to as 'SEBI') conducted an investigation into the alleged price manipulation in the scrip of SFL, during the period October – December, 1999. It was seen that there was unusual upward price movement in the shares of SFL during this period, the price having moved up from Rs. 8 to a high of Rs. 38. Similarly, it was also seen that the volumes in the shares, which were traded a total of 7 times in the whole year, prior to 26.10.99, had gone up significantly during the investigation period.
3. Investigations revealed that one Shri Mahendra Shah, who was subsequently appointed the Managing Director of the company, was the largest seller during the investigation period. It was observed that Shri Shah had created artificial volumes in the shares of SFL and had then offloaded a large quantity of shares in the market. It was also seen that Shri Shah had put in large buy orders to influence the price of the scrip and had created false/misleading appearance of demand/interest in the shares of SFL, thereby influencing the share price of the scrip.
4. As a part of investigations into the price manipulation of the shares of SFL, SEBI had looked into the roles of various brokers and sub-brokers who had dealt in the shares of SFL during the relevant period. One such broker was M/s Amce Shares and Stocks Pvt Ltd (hereinafter referred to as "Acme"), a corporate member of BSE, who had traded in the scrip on behalf of its sub-broker MS Consultancy (hereinafter referred to as "MSC"), the details of which are as follows :

Settlement no	Purchases	Sales	Gross	Net
35	200	200	400	0
36	2500	27700	30200	-25200
37	14700	18000	32700	-3300
40	0	500	500	-500
Total	17400	46400	63800	-29000

5. MSC had in turn traded, as above, for its client Shri Viraj Gandhi. In order to ascertain the details of the above transactions and also to determine the role of MSC/its client in the price manipulation of the shares of SFL, if any, summons were issued by the Investigating Authority, advising them to appear before the Authority. However, neither MSC nor Sri Viraj Gandhi appeared before the Investigating Authority.
6. In view of the above, it was alleged that Acme, being the broker for MSC and hence being responsible for all acts, omissions and commissions of its sub-broker, MSC, had failed to exercise due skill, care and diligence and had violated the provisions of clause A (2) of Code of Conduct as prescribed under Schedule II read with regulation 7 of Securities and Exchange Board of India (Stock Brokers and Sub Brokers) Regulations, 1992 (hereinafter referred to as "Broker Regulations").

ENQUIRY PROCEEDINGS

7. Having considered the investigation report, Chairman, SEBI, vide order dated 24th July 2003, appointed an Enquiry Officer (hereinafter referred to as "Enquiry Officer") to enquiry into the alleged violations committed by Acme.
8. In accordance with the provisions of regulation 13 (1) of the Securities and Exchange Board of India (Procedure for holding Enquiry by Enquiry Officer and imposing penalty) Regulations, 2002 (hereinafter referred to as "the Regulations"), after having given an opportunity of personal hearing to Acme, the Enquiry Officer submitted a report dated 31st March 2004, to SEBI, with the recommendation that a minor penalty of warning be imposed on Acme.

SHOW CAUSE NOTICE AND REPLY

9. Subsequent to receipt of the Enquiry Report, as per regulation 13 (2) of the Regulations, a show cause notice dated 5th April 2004 was issued to Acme.

10. Acme, vide letter dated 27th April 2004, responded to the said show cause notice, pointing out that Enquiry Officer had not found them guilty of being a part of manipulative deals. Acme also pointed out instances where Enquiry Officer had agreed that investigation report had not brought out misconduct of Acme and had stated that non-response of MSC can not be attributed to Acme. Also, Acme pointed out that Enquiry Officer had opined that the act of Acme did not warrant suspension or cancellation of certificate of registration, but at the same time Acme can not be absolved from all responsibility and had suggested that Acme should be warned to be careful in future.
11. Acme submitted that the trades in SFL were in the normal and ordinary course of business and the volume/value therein was miniscule compared to their then prevailing total volume/value or transactions. Acme added that MSC was an old client and had always met its financial obligations to Acme.
12. Acme further submitted that sub-brokers are by and large independent, bound by a separate code of conduct under Broker Regulations and as such responsible for their business decisions. Main brokers of an exchange are liable for fulfillment of contractual liabilities of the market trades and they do not interfere in the routine business of the sub-broker except advising on risk management. Therefore, sub-brokers, who get separate registration directly from SEBI, own the responsibility of compliance with regulatory provisions and are independently liable for violations thereof and that sub-brokers are accountable for their acts of omission and commission.
13. Therefore, in the given circumstances, since the transactions in SFL scrip were carried out for and on behalf of MSC, Acme, as main broker can not be held responsible for violations, if any, relating to the transactions belonging to and accounted for on MSC's account. Acme further submitted that Enquiry Officer had considered non-compliance of summons by MSC to be an adverse point against Acme whereas SEBI had already initiated separate proceedings against MSC. In the business model followed by brokers, the sub-brokers, in terms of sub-broker-client agreement, have direct privity with their constituents. Acme had, on its part, furnished full details and particulars and also attended the hearing along with Sri Mahendra S Thakkar of MSC. It was submitted that it was on account of Acme's persuasive efforts that Sri Mahendra S Thakkar attended the hearing before the investigation team. Hence, Acme could not be faulted on any count and there was no wrong doing its part. Acme denied the charge of having failed to exercise due skill, care and diligence or having violated the provisions of Code of Conduct as given under Broker Regulations. Acme added that the very fact that it had carried out MSC's transaction, which were very small in volume/value and which were delivery based, bore testimony to its dexterity and skill of its management.
14. In view of the above submissions, Acme requested SEBI not to impose minor penalty of warning, as recommended by Enquiry Officer, as the charge against it was trivial, the violation being technical and general in nature.

CONSIDERATION OF ISSUES AND FINDINGS

15. I have carefully considered the facts of the case, the findings of the Enquiry Officer, the reply of Acme to the show cause notice and other material on record. My findings with respect to the allegations against Acme are as under.
16. I have observed that Acme had traded in the shares of SFL in 4 settlements, the gross volume being 63,800 shares. However, I have also observed that all these trades were done for their sub-broker MSC and that Acme did not have any proprietary trades in SFL.
17. I have also noted the following observations of the Enquiry Officer :
 - i. The transactions entered on behalf of MSC were delivery based.
 - ii. MSC had stopped transacting for Shri Viraj Gandhi.
 - iii. There is no allegation regarding Acme being involved in any manipulative trading.
18. However, at the same time, I have also observed that MSC , sub-broker of Acme, failed to respond to the summons issued by the Investigating Authority, seeking to ascertain the facts of the case. The failure of MSC and its client, who had traded significantly in the shares of SFL, hampered the investigation process of SEBI. Acme, being the broker for MSC, is liable for all acts and deeds of MSC. I have noted the submission of Acme that sub-brokers are independent entities, responsible for due diligence, control of their clients and business decisions and that sub-brokers are bound by separate code of conduct; also that a broker can not be made liable for the acts of sub-broker.
19. Although I tend to agree with the submission that sub-brokers are responsible for their own clients and trading decisions, I have also noted that affiliation to a registered broker is a pre-condition for registration as a sub-broker, along with the requirement of a tripartite agreement between broker, sub-broker and its client. The existence of this requirement clearly signifies the symbiotic relationship between a broker, a sub-broker and the ultimate client. That being the case, Acme can not deny all responsibility towards the acts of its sub-broker.

20. In the instant case, MSC had traded for its client through its broker Acme. Acme had knowledge of trades taking place at MSC's end. The kind of trading that MSC was doing should have alerted Acme, particularly in view of the fact that the same client was trading in the shares of both SFL and Sawaca Communications (related companies), both of which were illiquid scrips till before the relevant period. It can not be claimed that a sub-broker is exclusively responsible for its client; even the broker is under obligation to keep himself abreast of the activities of the sub-brokers' clients. If Acme's argument of broker not being responsible for sub-broker is accepted, then the whole purpose of tripartite agreement is lost.
21. Acme had pointed out that Enquiry Officer had opined that non-response of MSC to the summons of the Investigating Authority can not be attributed to Acme. However, Enquiry Officer had also observed that the broker can not disown the responsibility for the action or in action of sub-broker.
22. In view of the facts and circumstances of the case, I agree with the Enquiry Officer in that Acme had not been careful while dealing with its sub-broker MSC and its client, thereby violating the Code of Conduct as given under Schedule II read with regulation 7 of Securities and Exchange Board of India (Stockbrokers and sub-brokers) Regulations, 1992.

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23. Therefore, in exercise of powers conferred upon me in terms of Section 19 of the Securities and Exchange Board of India Act, 1992, read with regulation 13 (4) of Securities and Exchange Board of India (Procedure for holding Enquiry by Enquiry Officer and imposing penalty) Regulations, 2002, I hereby impose a penalty of warning on Acme Shares & Stock Pvt Ltd., member, BSE. I also direct the broker to note that any instances of violations or non-compliance of the Securities and Exchange Board of India Act and the Rules and Regulations, in future, shall be dealt with more stringently.

Place: Mumbai

Date: October 6th , 2004

A K Batra

Whole Time Member

Securities and Exchange Board of India