

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

UNDER REGULATION 13(4) OF SEBI (PROCEDURE FOR HOLDING ENQUIRY AND IMPOSING PENALTY BY ENQUIRY OFFICER) REGULATIONS, 2002

AGAINST CFL SECURITIES LTD., MEMBER, THE NATIONAL STOCK EXCHANGE (REG NO.INB 230629433)

1. Investigations were conducted by SEBI into the unusual price rise and volumes in the scrips of Ravalgaon Sugar Farms Ltd (hereinafter referred to as Ravalgaon) and Shrenuj & Co Ltd (Shrenuj). The price of Ravalgaon had risen by 41.77%, from Rs.3220/- on 23.5.2001 to Rs.4565/- on 19.6.2001 with fluctuating volumes. Similarly, price rose by 10.75% from Rs 39 on May 04, 2001 to Rs 43.7 on May 14, 2001 in Shrenuj also.
2. On examination of the data of trade log and order log, SEBI noticed possible violations of the provisions of SEBI Act, 1992, SEBI (Stock Brokers and Sub Brokers) Regulations, 1992 [hereinafter referred to as SEBI (Stock Broker Regulations)] and SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Markets) Regulations, 1995 [hereinafter referred to as SEBI (FUTP) Regulations] by M/s CFL Securities (hereinafter referred to as 'CFL'), a member of National Stock Exchange (NSE). It was found to have executed structured deals in violation of SEBI circular dated 14.09.'89 and also have created artificial volumes in violation of SEBI (FUTP) Regulations in both the aforementioned scrips.
3. Pursuant to the investigation, enquiry was conducted under SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 [hereinafter referred to as SEBI (Enquiry) Regulations] the possible violations as aforesaid by CFL. On completion of the enquiry, the Enquiry Officer (hereinafter referred to as E.O.), arrived at the finding that CFL has indulged in structured deals and created artificial volumes in the scrips of Ravalgaon and Shrenuj, violating regulations 4 (b),(c) & (e) of SEBI (FUTP) Regulations and failed to exercise due diligence in the conduct of business in violation of the provisions of clauses A(1), A(2), A(3) and A(4) of the Code of Conduct for Stock brokers specified in Schedule II read with Regulations 7 of SEBI (Stock Brokers and Sub-brokers) Regulations, 1992.

On the basis of aforesaid findings, the E.O. recommended suspension of certificate of registration of CFL for a period of 6 months.

SHOW CAUSE NOTICE

4. A show cause notice was sent to CFL on July 20, 2004 wherein while communicating findings of enquiry officer, they were asked to show cause as to why the action as may be considered appropriate should not be taken against them.

REPLY

5. Vide its reply dated July 30, 2004 CFL submitted as under:
 - a. That they have executed couple of transactions in the scrip of Ravalgaon Sugar Farms Ltd and Shrenuj & Co. Ltd during the period May 4, 2001 to June 29, 2001 with their group associates and clients only to arrange temporary funding to meet their obligations at NSE/BSE.
 - b. That they did not have intention, at any point of time during those transactions to create artificial volume. The volumes so created were incidental due to the repeated transactions done for the purpose of funding.
 - c. That they were not benefited by doing those transactions. There was an attempt to survive in the midst of hardships.
 - d. That they have not sold any of these shares at a higher price than the buy price, and as such no investor suffered any loss due to those transactions.
 - e. That they used the payment received from Aditi A.Dalal (which they received through D.G.P.Securities/Ashadevi Beriwalla), for meeting the pay-in obligations at NSE from time to time). While furnishing the copy of relevant bank statements they gave following examples in support of their submissions :
 - i. On 15.05.2001, CFL/Tropical received Rs.90 lacs from Aditi Dalal who in turn had received this money from D.G.P.Securities Ltd on behalf of Ashadevi Beriwalla which was used for their NSE pay-in on account of CFL Securities.
 - ii. On 12.6.01, CFL/Tropical received Rs.85 lacs from Aditi A.Dalal who in turn had received this money from D.G.P.Securities on behalf of Ashadevi Beriwalla which was used for their NSE pay-in on account of CFL Securities.

iii. On 26.6.01, CFL/Tropical received Rs.80 lacs from Aditi a Dalal who in turn had received this money from D.G.P.Securities on behalf of Ashadevi Beriwalla which was used for their NSE pay-in.

- f. That, at some point of time the cycle of repeated transactions had to come to an end. Ultimately they were not able to fulfill the pay-in obligation of the NSE settlement on 16th October 2001 and due to the same, their NSE terminal was deactivated on October 16, 2001.
- g. That the pay-out of shares including Ravalgaon Sugar Farm Ltd and Shrenuj & Co. Ltd were retained by NSE and they sold the shares directly to settle all dues of CFL towards pay-in obligations. Further, while enclosing a statement showing the total shares or Ravalgaon & Shrenuj sold by NSE after October 16, 2001 and statements of Final Obligations & Final Delivery for the settlement through which shares were directly sold by NSE, it was submitted that this statement, will prove that their intention for doing these transactions was only to make temporary funding and not to create artificial volumes or price rigging or any type of fraudulent manipulation in the stock market.
- h. That NSE has already levied monetary penalty on CFL for the transactions done in the scrip of Ravalgaon Sugar and Shrenuj & Co.
- i. That they are suffering several hardships and their NSE/BSE terminals have already been deactivated since October/November, 2001, and since then they are out of all stock broking activities.
- j. That they were facing financial crisis, and most of it have been resolved and they are in the process of clearing off all their liabilities.
- k. That they had no intentions of violating the provisions of SEBI. They entered into these transactions for their survival. They requested for condoning the violations.
- l. That no action as recommended by EO be taken against them as they were out of business for about 3 years, bearing heavy losses and passing through severe hardships.

While requesting that their registration may not be cancelled as recommended by EO, they brought on record that there were certain contradictions between the show cause notice and the letter summarizing the recommendations of EO.

FINDINGS

- 6.0 I have carefully considered the findings of the Investigation Report, Enquiry Report, Show Cause Notice and reply received from CFL. I also find that the Member has never sought any personal hearing and therefore I shall proceed on the basis of record as aforesaid.

A) IN THE SCRIP OF RAVALGAON SUGAR FARMS LTD.

- 6.1 I find that price of Ravalgaon at NSE had risen from Rs.3220/- on 23.5.2001 to Rs.4565/- on 19.6.2001 with fluctuating volumes. On June 11 and 15, 2001 the volume in the scrip was 314 shares and 1240 shares at NSE respectively. During the investigation period between May 04, 2001 to June 29, 2001, 1978 shares were traded at NSE. CFL, I find, has executed trades in the scrip in its own account and also on behalf of Globex Finance Services, the details of such trading as extracted from the finding of investigation are as under:

SN	Date of Trading	Client Name	Buy Qty	Sell Qty	Client Gross Qty	% of Client Gross to Mkt Gross	Client Net Qty	% of Client Net to Mkt Net
2001023	11.6.01	Own A/c	310	0	310	35.23	310	81.58
2001024	15.6.01	Own A/c	1240	0	1240	48.40	1240	153.47
2001024	15.6.01	Globex Fin Ser.	0	450	450	17.56	(450)	(55.69)

- 6.2 I find that all the above trades are executed as structured deals between CFL and another broker namely, DGP Securities Ltd. As seen from the above table, on June 15, 2001 the total volume of 1240 shares was created by CFL. Out of which trade for 450 shares was done through a cross deal for which the selling client was Globex Financial Services Ltd. I find that CFL has also executed structured deals for 310 shares with the above broker on June 11, 2001 when the market volume of scrip was 314 shares.

- 6.3 I find, that on October 22, 2003, during the recording of the statement of representative of CFL Securities, trade and order log of NSE was shown to them by the SEBI officials. On a close scrutiny of the trade log and order log, I find that when the buy order entry time was 11:47:57, the sell order entry time was 11:47:56. The timings of both buy and sell orders against the respective dates are detailed below:

Sr.No.	Date	Buy Order Entry Time	Sell Order Entry Time
1.	June 11, 2001	11:47:57	11:47:56

2.	June 15, 2001	12:51:10	12:51:10
3.	June 15, 2001	13:03:57	13:03:56
4.	June 15, 2001	13:52:20	13:52:20
5.	June 15, 2001	14:34:44	14:34:44

In all the above transactions the buying member was CFL Securities and the selling member was DGP Securities Ltd. Thus, it is seen that all the transactions mentioned above were matched between the buying and selling members. Such matching of transactions is not possible without prior understanding between the two parties. Such structured deals and cross deals tamper with the free and transparent price discovery mechanism of the exchange and thus are prohibited vide SEBI Circular dated 14.9.94.

- 6.4 The details of the volumes, the prices at which the aforementioned trades had been executed and the total percentage to market gross of the trades executed by CFL are as under :

SN	Date of trading	No. of trades	Avg. trd price (Rs.)	Trd Qty (shares)	% to Mkt Gross for the SN
2001023	11.6.01	1	4825	310	35.23
2001024	15.6.01	4	4712	790	30.83
Total		5		1100	

I find that these trades have been placed at the same price and approximately at the same time. I note that all the deals have been executed by CFL on its own account on the buy side and Ashadevi Beriwal, its client on the sell side. Further, I note that 1100 shares of Ravalgaon were transferred to the account of Aditi Dalal even though the trades were executed on CFL's own account. The details of such trades as extracted from the findings of investigation are as under:

SN	Date of trading	Net buy of broker	Client Name	Client Net Buy	Client Demat Account Particulars	Securities delivered to/Recd from	Qty delivered/ Recd	Particulars
2001023	11.6.01	310	CFL SEcs Own A/c.	310	104050810 UTI Bank	Transfer to Aditi Dalal's a/c	310	310 shares due to CFL Secs credited to Aditi Dalal's a/c
2001024	15.6.01	790	CFL SEcs Own A/c.	790	104050810 UTI Bank	Transfer to Aditi Dalal's a/c	790	790 shares due to CFL Secs credited to Aditi Dalal's a/c

- 6.5 I find that all the shares of Ravalgaon sold on behalf of the client of CFL, viz., Ashadevi Beriwal were transferred to the pool account of CFL from the beneficiary account of Aditi Dalal who is the wife of one of the director of the CFL, Shri Asim B Dalal. Thus, it is observed that the shares were moving from the account of Aditi Dalal for pay-in to the exchange. During the same settlement, when pay-out was received from the exchange, the shares were moving back to the same account.

I find that Shri Milan Dalal, Director of CFL in his statement dated October 21, 2003 before the investigating officer and his reply dated July 30, 2004 also has stated that the reason for the structured deals was to obtain funds to meet their NSE valan obligations and these transactions were part of their efforts to survive in the midst of hardships and obstacles. The explanation of Milan Dalal is not acceptable. As observed earlier such structured deals tamper with free and transparent price discovery mechanism and same is prohibited in view of Circular dated 14.9.99. Such deals cannot be allowed for raising funds or for any other purpose.

I find that Aditi Dalal sold 1100 shares to Ashadevi Beriwal in 2 off-market deals. I also find that CFL used to receive money from Ashadevi Beriwal through Aditi Dalal against the sale of shares by Aditi Dalal to Ashadevi Beriwal. The same numbers of shares were received by the CFL through the market by matching the orders with the broker viz., DGP Securities Ltd. I find that the deal was executed through the market only and the orders were matched for this trade to take place so that the CFL could get the shares from Aditi Dalal only and the money also is paid to her only but through the

market mechanism. Thus it is clear that the shares received as pay out by CFL were being transferred to Aditi Dalal's account and the shares given as pay-in by DGP Securities Ltd. were being transferred from Aditi Dalal's account instead of being transferred from the client Ashadevi's account. It is also observed that the pay in obligations of DGP Securities is equal to the pay out obligations of CFL Securities Ltd.

- 6.6 From the above, I find that CFL has executed structured deals in the scrip of Ravalgaon and created artificial volumes in the said scrip and thus violated Regulations 4(b), 4(c) and 4(e) of SEBI (FUTP) Regulations and has also failed to exercise due diligence in the conduct of business as per the provisions of clauses A(1), A(2), A(3) and A(4) of the code of conduct for brokers specified in Schedule II read with Regulation 7 of SEBI (Stock Broker Regulations). I, therefore, hold CFL guilty for violation of provisions of the above Regulations.

I have also taken note of the admission of CFL that various transactions entered into by them with other group associates and clients was to create temporary funding arrangement to meet their NSE valan obligations. It has further stated that the intention was not to create false and artificial volumes to mislead the trading pattern. It has also stated that the transactions were part of their efforts to survive in the midst of hardships and obstacles.

B) IN THE SCRIP OF SHRENUJ & CO. LTD:

- 7.0 I find that CFL has not disputed its transaction in the scrip of Shrenuj. In this case also, their explanations are similar, viz., the said transactions were entered into to create temporary funding arrangements to meet their NSE valan obligations and it was a part of their efforts to survive in the midst of hardships and obstacles, I find that CFL has traded in the scrip of Shrenuj & Co. Ltd. both on its own account and on behalf of Aditi Dalal. The details of such trades are as under:

SN	Client Name	Buy Qty	Sell Qty	Client Gross Qty	% of Client Gross to Mkt Gross	Client Net Qty	% of Client Net Mkt Net
2001018	Aditi Dalal	390	0	390	9.25	390	30.66
2001019	Aditi Dalal	4177	500	4677	5.17	3677	8.32
2001019	Own A/c	40000	0	40000	44.24	40000	90.47
2001020	Aditi Dalal	2485	0	2485	14.01	2485	36.22
2001021	Aditi Dalal	400	0	400	10.52	400	37.45
2001022	Aditi Dalal	250	0	250	0.20	250	0.41
2001022	Own A/c	61000	0	61000	49.28	61000	98.96
2001023	Aditi Dalal	652	0	652	11.97	652	29.42
2001024	Own A/c	52000	0	52000	48.73	52000	97.52

- 7.1 I find that CFL has also executed 13 structured deals in the scrip of Shrenuj involving 1,53,000 shares with the broker DGP Securities Ltd., the details of such structured deals are as under :

SN	No of trades	Avg trd price	Trd Qty	% to Mkt Gross for the SN	% to Mkt Gross for the period
2001019	6	40.08	40000	44.24	11.36
2001022	3	40.07	61000	49.28	17.32
2001024	4	38.36	52000	48.73	14.77
Grand Total	13		153000		43.45

- 7.2 I find that the orders for the above trades were placed at the same price and approximately at the same time which is possible only if such trades are executed with prior understanding. The buy and sell order timing against the respective dates when they were placed are mentioned hereunder:

Sr.No.	Date	Buy Order Entry Time	Sell Order Entry Time
1.	May 14, 2001	10:43:17	10:43:17
2.	May 14, 2001	10:43:32	10:43:32
3.	May 14, 2001	10:50:58	10:50:59
4.	May 14, 2001	10:51:11	10:51:11
5.	May 14, 2001	10:51:33	10:51:33
6.	May 14, 2001	10:51:46	10:51:46

7.	June 4, 2001	11:30:09	11:30:08
8.	June 4, 2001	11:30:20	11:30:20
9.	June 4, 2001	11:30:34	11:30:34
10.	June 15, 2001	12:12:18	12:12:17
11.	June 15, 2001	12:12:32	12:12:31
12.	June 15, 2001	12:12:56	12:12:56
13.	June 15, 2001	14:54:58	14:54:58

- 7.3 I find that CFL was on the buy side and DGP Securities on the sell side. I find that the above structured deals accounted for 43.45% of the gross quantity traded in the scrip of Shrenuj during the period. I find that the shares due to CFL were credited to the account of Aditi Dalal and Harbinger Trading Co. Pvt. Ltd., an associate company of CFL. The same has not been denied by CFL.
- 7.4 I find that the shares of Shrenuj are moving from the account of Aditi Dalal for pay in on the exchange. During the same settlement, when pay out was received from the exchange, the shares were moving back to the same account. I find that Shri Milan Dalal, director of CFL, in his statement before the investigating officer as well as in his reply to the show cause notice has stated that the basic requirement at the time was only to obtain funds for meeting the NSE pay in obligations.
- 7.5 As seen from the details given above, CFL executed the trades in the scrip of Shrenuj through the market by matching the orders with those of the broker DGP Securities Ltd. Enquiry Proceedings are pending against DGP Securities. I have examined the price-volume data and I find that the traded volume in the scrip of Shrenuj was high on such days when the broker, CFL Securities had traded. It is also stated by CFL Securities, even in his reply to the show cause notice, that he has used the system for arranging temporary funding and creation of volumes were only incidental due to their repeated transactions.
- 7.6 Thus it is clear that CFL created artificial volumes in the scrip which were not genuine. One of the main reasons for treating artificial creation of volumes, as manipulative, is that, it induces innocent investors to trade in the securities on the basis of transactions which are not genuine, thereby misleading them and making them vulnerable to suffer wrongful losses. Thus, it is clear that the CFL has indulged in structured deals and created artificial volumes in the scrip of Shrenuj & Co. and thus has violated Regulations 4(b), 4(c) and 4(e) of SEBI (FUTP) Regulations. I also find that it has failed to exercise due diligence in the conduct of business as per the provisions of clauses A(1), A(2), A(3) and A(4) of the code of conduct for brokers specified in Schedule II read with Regulation 7 of SEBI (Stock Broker Regulations). I, therefore, hold CFL guilty for violation of provisions of the above Regulations.
- 7.7 I have noted that vide their reply dated July 30, 2004, CFL has stated that the findings of E.O and the communication to them about the same in the show cause notice are different. It is observed that on the basis of his findings, EO had recommended suspension of the registration of the member for a period of six months. However, in the course of enquiry, when EO was apprised that the terminals of CFL Securities at NSE and BSE have been deactivated by respective exchange, he made a conditional recommendation for cancellation of the registration of member. In this regard, I have found that the member has applied for surrender of membership to NSE and the same is pending clearance with SEBI.
- 7.8 From the above, it is seen that CFL has indulged in the violations of SEBI circular, SEBI (FUTP) Regulation and SEBI (Stock Broker Regulations). I find that CFL has admitted that such transactions were to create temporary funding arrangements to meet their NSE valan obligations and was part of their efforts to survive in the midst of hardships and obstacles. It has further submitted that their NSE terminal has been deactivated since 16th October 2001 and they are out of business since then. It was also submitted that NSE has levied a penalty of Rs.25,000/- each for transactions done in the scrip of Ravalgaon & Shrenuj and therefore no action may be taken by SEBI. Having considered their submissions I am of the view that action taken by NSE against its member does not preclude SEBI from taking action against the intermediary for violation of its Regulations.
- 7.9 I find that the E.O has made another recommendation that if the exchange has expelled the member after deactivation of terminal and the member has not been re-admitted after expiry of six months of expulsion, the registration of the member shall be liable to be cancelled in such an eventuality. The member, I note has surrendered his membership at NSE, which is approved by the exchange, although clearance is pending with SEBI.
- 7.10 Taking into consideration all the facts and circumstances of the case and the findings as aforesaid, I, in exercise of powers conferred upon me under Section 4 of SEBI Act, 1992 read with SEBI (FUTP) Regulations, 1995 read with corresponding provisions of SEBI (FUTP) Regulations, 2003, SEBI (Stock Broker) Regulations and Regulation 13(4) of SEBI (Enquiry) Regulations direct that the certificate of registration granted to M/s CFL Securities be suspended for a period of six months.
7. 11 Meanwhile, the surrender of membership shall not be approved by SEBI, till CFL Securities completes the period of suspension. As M/s.CFL Securities Limited is not operative in the market and its terminal has been deactivated, this order

shall come into effect from the date of the order.

Mumbai

January 19, 2005

G. N.Bajpai

Chairman