

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER AGAINST M/s KABU INVESTMENT SERVICES, (PROPRIETOR: FEROZ S GANGJI) MEMBER PUNE STOCK EXCHANGE, SEBI REGISTRATION NO. INB 110252417 UNDER REGULATION 13(4) SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002 FOR THE IRREGULAR TRANSACTIONS IN THE SCRIP OF HOME TRADE LTD.

WTM/GA/33/ISD/11/05

1.0 **BACK GROUND**

1.1 M/s Kabu Investment Service (hereinafter referred to as the 'broker') is a member of the Pune Stock Exchange (hereinafter referred to as 'PSE') and is registered with the Securities and Exchange Board of India (hereinafter referred to as 'SEBI') as a Stock broker under Section 12 of SEBI Act, 1992 with Registration Number INB110252417.

1.2 The scrip of Home Trade Ltd.(HTL) was listed at Pune Stock Exchange(PSE) and Bangalore Stock Exchange(BgSE). The scrip was listed at Pune Stock Exchange on November 15, 1999 at Rs 250/- and at BgSE on November 16, 1999 at Rs.275. There was a very sharp price rise in the scrip both at PSE and BgSE. The prices reached Rs.315 within two weeks i.e. by December 06, 1999. Thereafter, there has been a burgeoning increase in the prices of the scrip as under:

Date	Price in Rupees
December 30, 1999	525.00
January 31, 2000	735.00
March 31, 2000	809.00
May 05, 2000	874.00

The maximum rise in the price of the scrip took place between November 16, 1999 and March 31, 2000 when the price moved from Rs.275 to Rs.815/-. Thereafter the price fell to Rs. 640/- in September 25, 2000. Subsequently, the face value of the shares changed to Rs. 2/- and the price went up from a level of Rs. 123/- on September 26, 2000 to Rs.171/- during February 2001. The scrip continued to trade at around Rs. 150/- till September 14, 2001 and thereafter in the range of Rs. 170/- till January 2002.

1.3 Thus during the period of investigation i.e. 1st April 2000 to December 2001 (hereinafter referred to as the period under consideration), two different periods of trading were identified as follows :

a) 1st April 2000 to 31st March 2001

Name of the Broker	Buy qty	% to the total vol. at exchange	Sell qty	% to the total vol. at exchange
Shrine Investments	153900	22.05	154400	22.12
Shoba Investments	143200	20.52	139500	19.99
Yatin Shah & Co.	122100	17.50	102300	14.66
Kabu Invest.Services	105900	15.17	105900	15.17
Trimty Invest.	75200	10.78	75200	10.78
Vinod Kumar Jaggnath	62100	8.90	62100	8.90
Amin Mulani	24600	3.52	44100	6.32
Total	687000	98.44	683500	97.44

From the above it is clear that these 7 brokers mentioned above have constituted about 98% of the total volume in this scrip at Pune Stock Exchange.

b) 1st April of 2001 to 31st December 2001

Name of the Broker	Buy qty	% to the total vol. at exchange	Sell qty	% to the total vol. at exchange
Shoba Investments	75100	17.59	75100	17.59
Yatin Shah & Co.	60300	14.13	56100	13.14
Kabu Invest.Services	47500	11.13	47500	11.13
Trimty Invest.	41100	9.63	41100	9.63
Shrine Investments	37400	8.76	39700	9.30
Kanchan Investments	34500	8.08	32400	7.59
Sharad B Shah	28600	6.70	24900	5.83
Clever Investments	21300	4.99	21300	4.99
Chirag Investments	19600	4.59	16400	3.84
CR Kulkarni	16700	3.91	16300	3.82
Ramesh G Shah	12300	2.88	13000	3.05
PL Pushpalakshmi C&C	13200	3.09	13100	3.07
Jagannath Vinod Kumar	5300	1.24	6300	1.48
Total	412900	96.72	401400	94.45

From the above it is clear that these 12 brokers mentioned above have constituted more than 90% of the total volume in this scrip at Pune Stock Exchange. It is also seen that brokers Shoba Investments, Shrine Investments, Yatin Shah, Trimty Investments and Kabu Investments have dealt in a major way during the period 2000 to 2001 and 1st April 2001 to 31.12.2001.

1.4 Investigation was conducted by SEBI into the affairs of buying, selling and dealings in the scrip of HTL by the members of PSE and BgSE including the said broker under the provisions of SEBI Act and its regulations. Investigations revealed that a

set of brokers at PSE and BgSE including the said broker were involved in creation of abnormally high volumes, circular trading, price manipulation and false markets thereby contravening the provisions of SEBI Act and regulations including SEBI (Stock Brokers and Sub-brokers) Regulations, 1992. Investigation brought out the role played by these brokers including the said broker in price rise during the period of investigation through a phalanx of clients introduced by the itinerant and trusted employees of HTL. It was also alleged that the broker failed to observe the 'Know Your Client' norms.

2.0 APPOINTMENT OF ENQUIRY OFFICER

- 2.1 On completion of investigations, enquiry officer was appointed vide order dated May 28, 2003 under Regulation 5(1) of SEBI (Procedure for Holding enquiry by enquiry officer and imposing penalty) Regulations, 2002 to enquire into the alleged irregular transactions of the broker in the scrip of HTL.
- 2.2 I have noted that a Show Cause Notice encompassing alleged violation of Clause A(2), A (3-4) and B(1) of Schedule II under Regulation 7 of SEBI (Stock Brokers and Sub Brokers) Regulations 1992; Clauses (a), (b), and (c) of Regulation 4 of SEBI (Prohibition of Fraudulent and Unfair trade Practices relating to Securities Market) Regulations 1995 was issued to the Broker under Regulation 6 (1) of the regulation, payment not being made and received by the clients, by the enquiry officer and that the broker submitted his reply and appeared for personal hearing. The enquiry officer conducted the enquiry in terms of the regulation and the broker was given a fair and reasonable opportunity to make his submissions.
- 2.3 After considering the reply and the submissions made, the Enquiry Officer submitted his report dated November 18, 2004. The Enquiry Officer observed that the broker contributed significantly to the traded volumes during the period under consideration in the scrip of HTL for clients viz. Shri Vishnukumar Savnani and Shri Narendra Kumar Jain, who were strangers and were introduced for the first

time by Mr Veerkar, an employee of HTL. Further, the broker did not assess their financial capabilities and networth while failing to exercise due diligence in admitting the clients. The Enquiry Officer recommended a minor penalty of ‘suspension of Certificate of Registration for a period one month under regulation 13(1) (a) (iv) of the regulation.

3.0 CONSIDERATION OF THE ENQUIRY REPORT

- 3.1 After considering the Enquiry report, a Show Cause notice dated November 25, 2004 under regulation 13(2) of the regulation was issued to the Broker enclosing therewith a copy of the Enquiry Report. The broker submitted his reply and comments on the enquiry report vide letter dated December 10, 2004 and further appeared for personal hearing on February 10, 2005 and made oral submissions.
- 3.2 Between April 1,2000 and March 31, 2001, the gross purchase and sales of the broker in the scrip contributed 15 and 11.3 % of the total volume in the scrip in the exchange .The details of purchase and sale by the broker in the scrip of HTL are given as under:

Period	Gross purchases	% to the total buy volume at the exchange	Gross sales	% to the total sell volume at the exchange
01.04.00 to 31.03.01	1,05,900	15.17	1,05,900	15.17
01.04.01 to 31.12.01	47,500	11.13	47,500	11.13

Broker’s main clients were Shri Vishnukumar Savnani and Shri Narendra Kumar Jain. It was admitted by Shri Feroz Gangji, proprietor of Kabu Investment vide his statement dated May 17, 2002, that the broker executed trades for the above named clients in the scrip of Home Trade Ltd and the clients were introduced by Shri

Rajendra Veerkar, an employee of HTL. Orders on behalf of the client were also placed by Shri Rajendra Veerkar. However, it was submitted by Shri Rajendra Veerkar vide his statement dated March 31, 2003 that the orders on behalf of the above clients were placed by Shri Himmat Singh Porwal and it was Shri Porwal who received the contract notes and made / received the payments on behalf of these clients.

3.3 The broker had executed following trades on behalf of the clients:

For the period from **01.04.2000** to **31.03.2001**

Client	Buy	Sell
Vishnukumar Savnani	53,100	53,100
Narendra Kumar Jain	49,510	49,510

For the period from **01.04.2001** to **31.12.2001**

Client	Buy	Sell
Vishnukumar Savnani	42,600	42,600
Narendra Kumar Jain	4,900	4,900

From the above table, it can be observed that all the transactions were squared off and did not result in deliveries. Having regard to the price of the scrip and significant value of these transactions, it is surprising that that the broker did not assess the financial networth of a client who had just started trading and that too only in the scrip of HTL.

3.4 The broker made the following submissions to the investigating Officer vide his statements dated May 17, 2002, August 02, 2002 and March 29, 2003:

- 1) That he had never met the clients and submitted that he had executed the transactions on behalf of the clients after receiving telephone calls from Shri Veerkar
- 2) That the clients were introduced by Mr. Veerkar.
- 3) All the payments were collected to / from Mr. Veerkar.
- 4) The margin money on behalf of the clients was received from Mr. Veerkar.
- 5) The client introduction forms and member client agreements of the said clients could not be traced.

It was submitted by the broker that client registration form and broker client agreement were obtained from the clients but these were misplaced. Since client registration forms and member client agreements of the said clients are not available, it cannot be said that the broker had assessed the financial capabilities of the clients, particularly having regard to the volumes traded by these relatively new clients.

- 3.5 The identity of the clients was not known to the broker yet he started trading as per the orders placed by Shri Veerkar. It was submitted that Shri Veerkar was introduced by Shri Amin Mulani, broker PSE but his address is not known to the broker.
- 3.6 In this connection, it would be relevant to refer to the order of the Hon'ble SAT in Madhukar Sheth Vs SEBI (Appeal No.46 of 2002). The following is extracted from the said order dated September 18, 2003:

“Before executing series of transactions for his client, any prudent broker would have gone a bit far to ascertain the goings around and also would have normally assessed the financial capability of the person for whom he was trading.....

.....The Appellant's submission that he had taken client registration form, entered into agreement etc.by itself was not sufficient. Exercise of due diligence in

ongoing transactions is a continuous process and it is not a one time measure to be adhered to while taking up the first transaction. The appellant's submission that it was B's dishonesty that created the problem did not absolve him of his failure to discharge his duties as a prudent broker.....

.....On the basis of the material available on record, it was difficult to conclude that the appellant had exercised due skill and care in dealing with 'B'. It was not that the appellant had carried on only few trade transactions for 'B' for a short period. He had transacted in huge volumes for 'B' and the association dated back to August 2000. If the appellant could not see any design or pattern in the transactions which 'B' was executing through the appellant during the period, then the appellant certainly deserved to be blamed for being indifferent and unconcerned and for that reason he was at fault for the failure to exercise due skill and diligence.....

.....It is true that a broker cannot act of his own against the instructions of the client. But no one can compel him to be a party to manipulate the market. No doubt a broker is supposed to protect the interest of his client, but he is also expected to protect the interest of the securities market in which he operates. It is his duty to ensure not to be a party to any market manipulation and that the market in which he operates is run on a healthy and non-manipulative basis."

- 3.7 From the materials on record, it emerges that all the clients were relatively new and hailed from far off place like Mumbai. Further, these clients traded significantly only in the scrip of HTL and contributed almost 15% and 11% of the volume traded at PSE respectively accompanied with a huge surge in price. Thus the trades executed by the broker for his clients are exorbitant and appear to be not innocuous transactions but one meant to rig the market as would be evident from the concentrated volume and sharp movement of price. It, therefore, cannot be said that the broker acted in good faith and with due diligence before considering of trading for these clients.

3.8 Considering the materiality of circumstances in their pith and essence and also in the context of what was happening in the market contemporaneously in relation to the scrip of HTL, the plea of innocence is not open to the broker, as he was fully aware of the goings on in the market and the manner in which the clients from a far away Mumbai were planted by the itinerant and the trusted employees of HTL in a manifest bid to jack up the price of HTL shares at PSE. The sequence of material happenings as adumbrated supra clearly establishes that the broker was part of the tout ensemble operating in the market to create a make believe volume and equally ensnaring price rise in the scrip. The factual matrix of the present case has to be appraised in the back drop of what was happening in the market in its murky dynamics as captured above and not in isolation, in as much as the named brokers allowed themselves to be used as a cat's paw by the wily employees of HTL for obvious market manipulation and this thread runs through and underpins the entire gamut of transactions that took place in PSE in the course of creating artificial market for HTL shares. In the brood of such material circumstances with their insightful portents as to the conduct of the market intermediaries playing the game at the behest of HTL employees, giving a short shrift to the time-tested and mandated requirements of KYC norms, due diligence, verification of financial capabilities and net worth of clients and a host of other reality checks meant to impart transparency and integrity to the market operations against any manipulative assemblage, the inexorable downside cannot be conjured away on the specious plea that the trade executed by the broker constituted a small proportion of the total trade. Any truncated view in such an extraordinary situation detracts a great deal from the gravity of irregularity, when the entire crafty and deceptive exercise of creating artificial market is seen as a whole, in all its manifestations, and with all the attendant consequences.

3.9 The trades by the broker constituted a significant percentage of the volumes at the exchange immediately after listing and during the period when there was unusual price rise in the scrip without change in economic fundamentals of the company.

The standard of proof required in a proceeding of this nature is at variance with the standard of proof required in criminal cases. It is sufficient if the preponderance of probabilities suggests towards the indulgence of the delinquent in the misconduct. The strict rules of Evidence Act and proof beyond reasonable doubt are not applicable to a proceeding of this nature. The Supreme Court's decision in Gulabchand vs Kudilal AIR, 1966, SC 1734 and the decision of the Special Court for trial of offences relating to transactions in securities in the matter of National Housing Bank versus ANZ Grindlays Bank, 1998 (2) LJ 153 is relied upon in this regard.

- 3.10 As regards obtaining the acknowledgements on the counterfoils of the contract notes, it was submitted that the same could not be maintained as the clients failed to return the acknowledged copies, hence the broker couldn't show acknowledged copy of the contract note. The explanation of the broker is not satisfactory. As it can be seen from the trading details, the number and the volume of transactions of the clients are significant. It is difficult to believe that there had not been a single instance where the broker could obtain acknowledged copy on the contract note. It is, therefore, concluded that the broker has violated Regulation 17(1) (i) of SEBI (Stock Brokers & Sub Brokers) Regulations, 1992.
- 3.11 The broker vide his reply dated December 10, 2004 reiterated his submissions before the enquiry officer as follows:
- a) All relevant transactions in the scrip of HTL were carried out only after receiving proper instructions from the clients and squaring off transactions were also done according to client's instructions.
 - b) 11% to 15% trading volume in PSE cannot be considered as high volume.
 - c) The broker has taken initial margin money from all the clients

- d) Shri Veerkar used to call the broker on behalf of the clients to place orders.
- e) Brokers of the PSE including the said broker do not have the mechanism as well as resources to monitor the scrip, hence prior knowledge cannot be attributed.
- f) During the relevant period the prices of scrip were already high, hence the allegation that the broker indulged in price rigging and creation of artificial volumes are not correct.

The broker has disputed the finding of the enquiry officer regarding violation of Regulation 17(1)(i) of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992. He submitted that the Enquiry Officer failed to consider the replies filed by the broker from time to time. I find no merit in both the above contentions. All other grounds raised in the reply were considered by the Enquiry Officer.

3.12 During the personal hearing held on February 10, 2005 the broker remonstrated that the allegations against him are technical in nature, hence punishment of suspension for a period of one month will result in his civil death. The broker assured that in future he will be more prompt and careful. He further submitted that the punishment is harsh and requested for leniency.

3.13 I note that while recommending the minor penalty of suspension of certificate of registration for a period of one month, the enquiry officer has considered the submissions made by the broker during the course of hearing. Therefore, I agree with the recommendations of the Enquiry Officer that the trades executed by the broker for the clients, who were introduced by an employee of HTL, resulted in abnormally high volumes of over 15 % and 11 % traded at PSE respectively during the periods under consideration. This led to the creation of false market in the scrip of HTL coupled with surge in price of HTL. Further, failure of the broker to exercise due care and diligence in his dealings with the clients, who were

introduced by the employees of HTL, allowed excessive speculation and creation of false market in the scrip of HTL. Thus broker has violated the provisions of Clause A(2), A (3-4), B(1) of Schedule II under Regulation 7 of SEBI (Stock Brokers and Sub Brokers) Regulations 1992; Clauses (a), (b), and (c) of Regulation 4 of SEBI (Prohibition of Fraudulent and Unfair trade Practices relating to Securities Market) Regulations 1995.

4.0 **ORDER**

Now, therefore, in exercise of powers conferred vide Regulation 13(4) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002, I hereby impose a minor penalty of suspension of certificate of registration for a period of one month in terms of Regulation 13(1)(a)(iv) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 on M/s Kabu Investment Services (INB 110252417), member Pune Stock Exchange.

This order shall come into effect on expiry of 21 days from the date of the order.

Place: Mumbai	G. Anantharaman
Date: 30-11-2005	Whole Time Member Securities and Exchange Board of India