

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 M/s. Triveni Management Consultancy Services Ltd, Member, INB 230652831, National Stock Exchange, Mumbai, in the matter of trading of scrip of M/s. Morepen Hotels Ltd

1.0 Background

1.1 In December 1995, Morepen Hotels Limited (hereinafter referred to as MHL) came out with a public issue at a premium of Rs.20/- per share. The scrip was listed at Jaipur Stock Exchange, Ludhiana Stock Exchange, Delhi Stock Exchange, National Stock Exchange (hereinafter referred to as "NSE") and The Stock Exchange, Mumbai (hereinafter referred to as "BSE"). There was a major spurt in the total volume in the scrip of MHL. From 29, 400 shares during January 2000 including nil volume for the entire month of July 2000, it shot up to 11, 34, 200 shares during the period August to November 2000. Further, the percentage of net quantity delivered to gross quantity traded during the period 11th September 2000 to 17th November 2000 was less than 1% of the total traded volume on the exchange. The same trend was accompanied by the price, the price of shares of MHL touched a 52-week high at Rs.285/- on 11th September 2000 and this was followed by a fall in price, a 52-week low, touching Rs.154.65 on 15th November 2000.

1.2 In view of the above, Securities and Exchange Board of India (hereinafter referred to as "SEBI") conducted an investigation into the trading of the scrip of MHL for the period June 2000 to December 2000 (hereinafter referred to as "investigation period"). During the investigation it was observed that the scrip of MHL was traded only at NSE and BSE.

1.3 It was observed that the P/E ratio of Morepen Hotels Ltd. was not in synchronisation with the rest of the hotel industry. The rise in volumes observed during the period June 2000 to December 2000 did not appear to be justified based on its fundamentals. SEBI's investigation into the matter found that 80% of the total quantity traded during the period June 2000 – December 2000 was contributed by few brokers of BSE and NSE. It was found that the ultimate clients had acted in concert through selected members and thus were involved in "circular trading".

1.4 The combined quantity traded in the scrip at BSE and NSE during the period June 2000 to December 2000 was approximately 38 lac shares out of which approximately 90% of the shares were traded by few entities at both the exchanges taken together.

1.5 It was observed during the investigation that during the investigation period M/s. Triveni Management Consultancy Services Ltd (hereinafter referred to as "TMCS"), Member of NSE, mainly engaged in the business of retail broking had traded in the scrip of MHL on behalf of a client, M/s. Vaibhav Laxmi Consultancy (hereinafter referred to as "VLC").

1.6 VLC started trading with TMCS sometime in August 2000. TMCS had taken a deposit of Rs.7.50 lac from VLC before starting to trade on behalf of VLC and allotted a trading terminal on September 2000. It was observed that trading pattern of VLC was to square off its positions at the end of each settlement. Based on the deposit received from VLC, TMCS was monitoring only the net outstanding position of VLC at the end of the day.

1.7 It was found during the investigation that the transactions executed by VLC were actually for M/s. S. M. Investment. By trading for a third party, VLC was acting as sub-broker to TMCS and was trading on behalf of (Proprietor Shamshad Sheikh, who is an employee with Jem Fiscal Ltd.) TMCS had dealt with VLC as sub-broker without registering VLC as its sub-broker.

1.8 It has been alleged that TMCS not showing due skill, care and diligence in its dealings with VLC in violation of 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 (hereinafter referred to as "Brokers Regulations"). Further, trading done by Sub-broker on behalf of the client was alleged to be in violation of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair trade practices relating to securities market) Regulations, 1995 (hereinafter referred to as "PFUTP Regulations").

2.0 Enquiry Proceedings

2.1 In view of the alleged irregularities committed by TMCS, Chairman, SEBI, vide his order dated 18th February 2002 appointed an Enquiry Officer (hereinafter referred to as "Enquiry Officer") to enquire into the affairs of TMCS. The Enquiry Officer after conducting the enquiry submitted a report dated 30th April 2004 to SEBI recommending a minor penalty of warning to be issued to TMCS.

3.0 Show cause notice and reply

- 3.1 Subsequent to submission of said Enquiry Report, a show cause notice dated 2nd June 2004 was issued to TMCS under regulation 13 (2) of Securities and Exchange Board of India (Procedure for holding Enquiry by Enquiry Officer and imposing penalty) Regulations, 2002, for which TMCS responded vide its letter dated 15th July 2004 inter-alia denying all the allegations made in the show cause notice. TMCS submitted that all the deals executed on behalf of VLC were on NEAT. The volume number of trades done by VLC was within the limit of its margin and there was no reason not to allow the client to deal in scrip of MHL and though the volume of trades done by VLC was substantial, the same was not enough to alarm TMCS. Based on the volume of trading done by the broker, a terminal was provided to VLC, which was regularly monitored and since NSE has not provided facility of setting a particular limit for each scrip hence it was not done. TMCS submitted that VLC was trading through TMCS in the capacity of client and it was not within the knowledge of TMCS that VLC in turn was trading on behalf of another client.
- 3.2 With regard to the allegation that VLC had squared off all its positions, TMCS submitted that VLC had deposited a sum of Rs.7.50 lacs at the time of starting the business with an understanding that net position during the settlement cycle will be allowed within the limits of margin and the excess position if any, had to be squared off. Squaring off of transactions was only limited to the extent of excess position and not total squared off.
- 3.3 With regard to the allegation that TMCS had not shown due skill and care in dealings with VLC, TMCS submitted that it has always maintained high standards of integrity, promptitude and fairness in the conduct of all its business.
- 3.4 With regard to the allegation of violating PFUTP Regulations, TMCS submitted that it had not effected, taken part in, or entered into either directly or indirectly, transactions in securities, with the intention of artificially raising or depressing the price of securities and thereby inducing the sale or purchase of securities by any person hence TMCS has not violated PFUTP Regulations nor has ever entered into any trade or activities which are prohibitory in nature and are in any way contrary to any of the Regulations or the Act. TMCS further submitted that all the sale and purchase of the shares of MHL was only on account of VLC and no other transactions were executed other than those done through NEAT. TMCS submitted that it had not taken part in any scheme or arrangement whereby a false market or volume is created in the scrip of MHL. The dealings done by the client through the broker in the scrip of MHL have not artificially raised or depressed the price of the scrip of MHL. As the purchase of the shares of MHL on behalf of VLC was over a period of time and the prices of the shares had also moved steadily, TMCS submitted it cannot be said that the purchase of shares was done with an intention to artificially raise or reduce the price of scrip of MHL. TMCS submitted that there were no pre-meditated, circular or non-genuine transactions which can be considered fraudulent, malpractice in nature.
- 3.5 TMCS contended that the enquiry officer has not established nor has provided any proof or sufficient reasoning to prove that TMCS was aware of VLC was dealing on behalf of third party as sub-broker without registering as sub-broker to TMCS.
- 4.0 Consideration of Issues
- 4.1 I have carefully considered the Enquiry Report, show cause notice issued to TMCS and submissions made in response to the show cause notice.
- 4.2 I observe that TMCS has admitted to have traded on behalf of VLC. Being a registered intermediary, TMCS is under positive obligation to be more diligent while dealing with clients, which TMCS failed to in the instant case resulting in violation of Brokers Regulations. The trading pattern of the client should have alerted TMCS and TMCS ought to have taken adequate steps to mitigate the trading strategy of the client. Functioning of TMCS calls into question the exercise of due diligence by TMCS and more so the intention of TMCS to comply with Broker Regulations in respect of due diligence, which is observed from the hands-off attitude of TMCS stating that there was no knowledge of VLC trading on behalf of a third party. I find that TMCS failed to exercise due skill and care in terms of Clause A (2) of the Code of Conduct prescribed for brokers, in Schedule II in terms of Regulation 7 of Securities and Exchange Board of India (Stock Brokers and Sub-brokers) Regulations, 1992.
- 4.3 I observe that the P/E ratio of MHL was not in synchronization with the rest of the hotel industry. Hence, neither the scrip price of MHL was justified based on the fundamentals of MHL nor the rise in volumes that were observed during the period June 2000 to December 2000. SEBI's investigation into the trading of the scrip of MHL found that 80% of the total quantity traded during the period June 2000 – December 2000 was contributed by few brokers of BSE and NSE. The scrip of MHL was clearly illiquid and TMCS being an intermediary should have had an idea of the same and suspected the trading pattern of VLC specially when VLC was squaring off transactions and not taking any deliveries.
- 4.4 From trading details collected from brokers of BSE and NSE, it was seen that some of the clients, who were linked / connected to each other in some way or the other were trading in the scrip both at BSE and NSE. They had enrolled as clients to both BSE and NSE members and traded simultaneously in the scrip of MHL during the investigation period. From the records obtained from different brokers of both the exchanges, it was observed that most of these clients had not paid any margin to the brokers for the trades executed by them. Further, they were squaring off their positions not only at the end of settlement but almost on the same day.

- 4.5 From the trading details supplied by the exchange, it was also observed that delivery based business in the scrip during the period 1st June 2000 to 31st December 2000 was less than 1% of the total trading volume on the exchange. It was also observed that during the period of investigations the total volume at both the exchanges BSE and NSE were almost same and had great degree of similarity both in prices and total number of shares traded per day. It was also observed that the same set of clients was trading at both the exchanges.
- 4.6 The volumes in the scrip started going up from the last week of August 2000 and the TMCS has traded for VLC around the same time. VLC had entered into speculative transactions without any genuine interest in giving or taking delivery of shares. This has resulted in creation of artificial volumes and price rise in the scrip which otherwise had no interest from the general investors. Unsuspected innocent investors would be trapped by such false appearance of trading in securities. This is detrimental to the interest of investors and the orderly development of the securities market. Any prudent broker should doubt the intentions of the client and stop trading for it.
- 5.0 Order
- 5.1 In view of the above discussion I am in agreement with the finding of enquiry officer and I find M/s Triveni Management Consultancy Services Ltd has violated Clause A (2) of the Code of Conduct prescribed for brokers, in Schedule II in terms of Regulation 7 of Securities and Exchange Board of India (Stock brokers and Sub-brokers) Regulations, 1992.
- 5.2 Therefore, I, 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 warn M/s. Triveni Management Consultancy Services Ltd and direct it to be more diligent in complying with the SEBI Act, Rules and Regulations framed there under. I also direct the Broker to note that any instances of violations or non-compliance of the Act, Rules and Regulations in future shall be dealt with more stringently.

Place: Mumbai
Date: 27 December 2005

Madhukar
Whole Time Member
Securities and Exchange Board of India