

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER AGAINST M/S HARIKRISHNA STOCKS PVT. LTD. , MEMBER, THE BANGALORE STOCK EXCHANGE LTD., UNDER REGULATION 13(4) OF SECURITIES AND EXCHANGE BOARD OF INDIA (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002 FOR THE IRREGULAR TRANSACTIONS IN THE SHARES OF HOME TRADE LTD.

WTM/GA/106/ISD/11/06

1.0 BACKGROUND

- 1.1 M/s Harikrishna Stocks Pvt. Ltd. (hereinafter referred to as the Broker) is a member of the Bangalore Stock Exchange Ltd. (hereinafter referred to as BgSE) and is registered with the Securities and Exchange Board of India (hereinafter referred to as SEBI) as a stock broker under section 12 of Securities and Exchange Board of India Act, 1992 (hereinafter referred to as the said Act) with registration number INB 081077431.
- 1.2 The shares of Home Trade Ltd. (hereinafter referred to as HTL) were listed at Pune Stock Exchange Ltd. (hereinafter referred to as PSE) on November 15, 1999 at Rs 250/- and at BgSE on November 16, 1999 at Rs.275/-. There was a very sharp rise in the price of the shares of HTL both at PSE and BgSE and it reached Rs. 315/- within two weeks of its listing, i.e. by December 06, 1999. Thereafter, the price of the said shares reached Rs.874/- on May 05, 2000. The maximum rise in the price of the shares of HTL took place between November 16, 1999 and March 31, 2000, when it moved from Rs.275/- to Rs.815/-. SEBI conducted an investigation into the buying, selling and dealings in the shares of HTL inter alia by the members (stock brokers) of BgSE including the Broker in respect of the alleged circular trading and price manipulation thereby contravening the provisions of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Markets) Regulations, 1995 (hereinafter referred to as the FUTP Regulations) and Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Regulations, 1992 (hereinafter referred to as the Broker Regulations). The investigation conducted by SEBI found that the Broker had traded in the shares of HTL on behalf of his clients, Shri. Prabhulal Paliwal (from Mumbai) and Shri Shahid Gori (from Udaipur) during the period April 01, 2000 to March 31, 2001. The total transactions executed by the Broker on behalf of the said clients in the shares of HTL during the said period are mentioned below:

Period	Gross Purchase (shares)	% to the total volume buy at BgSE	Gross Sales (shares)	% to the total volume sell at BgSE
April 01, 2000 to March 31, 2001	1,19,450	15.09%	1,22,250	15.36%

- 1.3 The client wise trade details (in the shares of HTL) are as under :

Name of the client	Buy quantity	Sell quantity
Shri. Prabhulal Paliwal	98,450	98,450
Shri. Shahid Gori	21,000	23,800

- 1.4 The investigation conducted by SEBI prima facie revealed that the Broker had resorted to circular trading with other members of BgSE, wherein the shares of HTL were traded amongst themselves, creating artificial volumes in the shares of HTL.

2.0 APPOINTMENT OF ENQUIRY OFFICER

- 2.1 SEBI appointed an Enquiry Officer, vide order dated May 28, 2003 , under regulation 5(1) of Securities and Exchange Board of India (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as the 2002 Regulations) to enquire into the alleged irregular transactions of the Broker in the shares of HTL. The following allegations were leveled against the Broker:

1. Clients were not known and the orders on their behalf were placed by Shri. Rajneesh/Shri Veerkar/ Shri Rakesh which is in violation of SEBI Circular No. SMD/POLICY/IECG/1-97 dated 11.02.97.
2. Did not obtain the acknowledgement of the client on the counterfoils of the contract notes issued which is in violation of Regulation 17(1)(i) of SEBI (SB&SB) Regulations, 1992.
3. Deliveries of shares of HTL were not given to the clients but to Shri Rajneesh or Shri Rakesh of HTL which is in violation of B(1) of the Code of Conduct as specified in Schedule II read with Regulation 7 of SEBI (SB&SB) Regulations, 1992.

4. It was alleged that the broker actively traded in the scrip of HTL and artificially created higher price and volumes in the scrip of HTL. The broker entered into transactions that were not genuine trade transactions. It was alleged that the broker contravened provisions of the Regulation 4(a)(b)(c) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995 and violated Clause A(3-4) of the Code of Conduct as specified in Schedule II read with Regulation 7 of SEBI (SB&SB) Regulations 1992”.

5) All the above mentioned are also in violation of Rule 4(b) of SEBI (SB&SB) Rules, 1992 and Clauses A(1), A(2) and A(5) of the Code of Conduct as specified in Schedule II read with Regulation 7 of SEBI (SB&SB) Regulations, 1992” .

2.2 The Broker furnished his reply and made his submissions before the Enquiry Officer. The Enquiry Officer conducted the enquiry in terms of the 2002 Regulations and, vide report dated December 30, 2004, the Enquiry Officer had recommended for the imposition of a minor penalty of suspension of the certificate of registration of the Broker for a period of 15 days.

3.0 CONSIDERATION OF ISSUES AND FINDINGS.

3.1 Based upon the recommendations of the Enquiry Officer, a show cause notice dated January 06, 2005 was issued to the Broker under regulation 13(2) of the 2002 Regulations, asking him to show cause as to why the penalty as considered appropriate should not be imposed upon him. A copy of the Enquiry Report was also forwarded to the Broker with the said show cause notice. As no reply was received from the Broker, vide letter dated February 13, 2006, SEBI had once again advised the Broker to file his reply to the aforesaid show cause notice. The Broker vide letter dated February 20, 2006 inter alia replied that he had never intended to defraud any investor or to abuse the system. The Broker stated that, in the course of the trading he might have committed minor mistakes without his knowledge. The Broker further requested to consider his case sympathetically and submitted that he shall ensure that his acts as a broker would always be of utmost integrity and honesty. The Broker also stated that he was not desirous of attending the personal hearing before SEBI.

3.2 I have perused the Enquiry Report, show cause notice issued to the Broker, his reply dated February 20, 2006 and other relevant materials available on record. As the Enquiry Officer had not recorded any specific findings in respect of the violation of the provisions of FUTP Regulations, I deal with the other alleged violations attributed to the Broker. The transactions made by the Broker on behalf of his clients in the shares of HTL are not disputed. The Broker also admitted that he might have committed minor mistakes without his knowledge.

3.3 The Broker submitted that in the case of his client, viz. Shri Prabhulal Paliwal, the client registration form was obtained one week after the commencement of trading as it was informed by the said client that the same was sent by post. I note that, in terms of SEBI Circular dated February 11, 1997, the stock brokers were advised to maintain a database [pertaining to 'Know Your Client' (KYC) norms/ guidelines] of their clients. SEBI, vide circular dated April 11, 1997, had once again advised the stock brokers to follow the circular dated February 11, 1997 and further advised that the brokers might seek additional information, if any, so as to satisfy themselves about the antecedents of the client and that it would be the responsibility of the stock brokers to provide for clients' details as and when need arises.

3.4 Though the client registration forms of both the clients were collected by the Broker (one of the said form was obtained after the commencement of trading) some of the information as required in the said forms, such as details of the introducer were not obtained by the Broker. I note from the submissions (mentioned in the Enquiry Report) of the Broker that he had started trading for Shri Prabhulal Paliwal before obtaining the client registration form. It was the case of the Broker that the said client had called him from Mumbai and had requested him to trade in the shares of HTL. In the circumstances of the case, as the aforesaid client was new and the instruction to trade in the shares of HTL was given by the said client to the Broker over phone from a distant place (Mumbai), the Broker should not have executed trades on behalf of such client before entering into the client registration form and especially without knowing the antecedent of such client. Such act of the Broker can not be taken lightly. The Broker should have exercised due skill and care and diligence while trading on behalf of his clients in the shares of HTL, as expected from a stock broker in terms of Clauses A(1) and (2) of the Code of Conduct specified in schedule III of the Broker Regulations. Further, in the absence of the details of the introducer in the client registration forms, it can not be ruled out that the clients were not properly introduced to the Broker. I note that the Broker had submitted before the Enquiry Officer that as he was new to the broking business he was not aware of the rules and whatever he had done was with a view to earn commission only. This submission of the Broker cannot be accepted as being a market intermediary the Broker was expected to know all rules, regulations, circulars etc. issued from time to time in relation to its business and he was obliged to comply the said requirements. Therefore, it is fairly established that the Broker had violated the SEBI circular dated February 11, 1997 in respect of the Know Your Client norms. Further, in terms of the Code of Conduct specified in Schedule II of the Broker Regulations, a stock broker shall not encourage sale or purchase of securities with the sole object of generating brokerage or commission.

3.5 I note that the annual income of the clients as given in the client registration form was Rs.60,000/- (Shri. Prabhulal Paliwal) and Rs. 1,10,000 (Shri Shahid Gori) . It is one of the precautionary measures of a stock broker to verify the financial capacity of his clients before executing the trades on their behalf, which is one of the checks under the Know Your Client norms/guidelines. When a stock broker fails to perform the said primary requirements and further, if he happens to be transacting on behalf of such clients without knowing their antecedents and financial capacity, he is putting the entire

system in jeopardy. It is worth mentioning that in the case of the client (Shri Prabhulal Paliwal), the Broker had started trading before entering into the Client Registration Form and without knowing the antecedents. I note from the client registration forms of the above clients (as mentioned above) that the annual income of the clients were comparatively low considering the price of the said shares and the substantial transaction made by the Broker on behalf of his clients. The Broker had failed to submit any material to suggest that he had verified the financial capacity of his clients. The assessment of financial capacity of the client can not be taken as irrelevant even when the trades were squared off. The Broker should have exercised due skill, care and skill while trading on behalf of his clients. The above acts of the Broker clearly establishes that the Broker had failed to assess the financial capacity (one of the requirements under the KYC norms) of the clients before executing trades on behalf of them in the shares of HTL.

3.6 In terms of the provisions of the Broker Regulations, a stock broker, without any delay shall issue the contract note to his client and in terms of regulation 17(1) (i) of the Broker Regulations, he has to maintain the counterfoils or duplicates of such contract notes. In the present matter, the Broker had traded substantially in the shares of HTL on behalf of his clients. However, he had failed to submit the copy of acknowledgment of counterfoils of contract notes. It can be seen from the trading details, that the Broker had executed several transactions of significant volume in the shares of HTL on behalf his clients. Despite of executing large transactions, the Broker had failed to obtain the acknowledgement copy of contract notes. The above act of the Broker does not appear to be a simple omission considering the trades (volume of the shares) executed by the Broker on behalf of his clients. Therefore, it is established that the Broker had violated regulation 17(1) (i) of the Broker Regulations.

3.7 In the facts and circumstances as detailed above, I do not find any reason to differ with the recommendation made by the Enquiry Officer.

4.0 ORDER

4.1 In view of the foregoing, I, in exercise of the powers conferred vide regulation 13(4) of (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002, hereby impose a minor penalty of suspension of the certificate of registration of M/s Harikrishna Stocks Pvt. Ltd. Member, The Bangalore Stock Exchange Ltd. (Registration number INB 081077431), for a period of fifteen days.

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

G. ANANTHARAMAN

WHOLE TIME MEMBER

SECURITIES AND EXCHANGE BOARD OF INDIA

Place : Mumbai

Date : 30-11-2006