

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA

CORAM: G. ANANTHARAMAN, WHOLE TIME MEMBER

ORDER

UNDER SECURITIES AND EXCHANGE BOARD OF INDIA (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002 AGAINST SMIFS SECURITIES LIMITED, MEMBER, CALCUTTA STOCK EXCHANGE ASSOCIATION LTD. IN RESPECT OF ITS TRANSACTIONS IN THE SHARES OF DSQ INDUSTRIES LIMITED.

WTM/GA/145/ISD/2/07

Date of Hearing: September 13, 2006

Appearances :

For noticee : Shri. Pesi Modi, Advocate,
Shri Joby Mathew Advocate
Shri Santosh Dadheech,
Shri Manish Ajmera

For Securities and Exchange Board of India: Shri B Rajendran, Deputy General Manager.

1.0 BACKGROUND

- 1.1 The shares of DSQ Industries Ltd. (hereinafter referred to as DSQ), are listed at the Calcutta Stock Exchange Association Limited (hereinafter referred to as CSE). DSQ Industries Ltd is stated to be a group concern of Shri Dinesh Dalmia, main promoter of DSQ Software Ltd. It was, inter alia noticed that the shares of DSQ were traded in significant volumes during the period December 2000 – March 2001.
- 1.2 Inter alia, in the above facts and circumstances, Securities and Exchange Board of India (hereinafter referred to as SEBI) conducted an investigation to look into the alleged manipulation in the shares of DSQ and to look into the possible violations of the provisions of Securities and Exchange Board of India Act, 1992 (hereinafter referred to as the Act), Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) 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).
- 1.3 The investigation conducted by SEBI inter alia found that SMIFS Securities Limited (hereinafter referred to as Broker), member, CSE and stock broker registered with SEBI (registration No. INB 030599931) had traded substantially in the shares of DSQ during the above period. The Broker had also inter alia executed cross deals for its clients, Hulda Properties and Trades Ltd. (hereinafter referred to as Hulda), an associate of DSQ and SMIFS Capital Markets Ltd. (the promoter company of the Broker) and Dhanavaridhi Concerns Ltd. on December 21, 2000. On January 9, 2001, the Broker had also executed cross deals for its clients SMIFS Capital Markets Ltd., Dhanavaridhi Concerns Ltd. and Maya Trade Links Ltd. It is further seen that on February 13, 2001 the total volume at CSE in the shares of DSQ was 3,25,000 shares and that the entire volume was due to the transaction done by the Broker in a synchronized manner with other members of CSE. SEBI investigation also observed that the Broker had executed cross deals on February 21, 2001 and further executed trades in the shares of DSQ on March 01, 2001.

- 1.4 Inter alia in the facts and circumstances, it has been alleged that the Broker has prima facie violated regulation 4 (a) to (d) of the FUTP Regulations.

2.0 APPOINTMENT OF ENQUIRY OFFICER

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- 2.1 SEBI appointed an Enquiry Officer, vide order dated July 24, 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 Enquiry Regulations) to enquire into the aforesaid alleged violations committed by the Broker while executing trades on behalf of its clients in the shares of DSQ. The Broker filed its reply and made submissions before the Enquiry Officer. The Enquiry Officer conducted the enquiry in terms of the provisions of the Enquiry Regulations and vide report dated July 22, 2004 recommended a penalty of warning to the Broker.

3.0 SHOW CAUSE NOTICE, REPLY AND HEARING

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- 3.1 Based upon the recommendation of the Enquiry Officer, a notice dated July 30, 2004 was issued to the Broker under regulation 13(2) of the Enquiry Regulations asking him to show cause as to why the penalty as considered appropriate should not be imposed upon it. A copy of the Enquiry Report was also forwarded to the Broker with the said show cause notice.
- 3.2 The Broker vide letter dated August 18, 2004 inter alia stated that it had not violated any of the regulations and further submitted that no penalty might be imposed on it. The Broker also stated that it would take all necessary precautions in future while dealing with its clients as specified in the code of conduct for the brokers. The Broker further requested SEBI to take a lenient view in the matter. SEBI vide letter dated January 27, 2005 further advised the Broker to file its reply to show cause as to why the appropriate penalty should not be imposed on it.
- 3.3 The Broker vide its letter dated February 4, 2005 inter alia submitted that it had done nothing which was improper or in violation of any rules and regulations laid down by SEBI and exchanges. In respect of the trades executed (4,48,000 shares) on December 21, 2000, the Broker stated that it had executed the trades for the respective clients on the online trading terminal of CSE from time to time. The selling client was Hulda and buying clients were Dhanbridhi Concerns and SMIFS Capital Markets Ltd. The Broker clarified that it had sold and bought 4,48,000 shares of DSQ in the said settlement.
- 3.4 The Broker urged that it had received a letter from Hulda for short delivery and thereafter it had informed the status of the deliver to SMIFS Capital Markets Ltd. as Hula had delivered only 62,000 shares of DSQ. The Broker added that on receipt of consent from the buying client i.e. SMIFS Capital Markets Ltd. the transaction for the balance quantity was squared off at the purchase rate itself. It had further submitted that there were no findings in the investigation report to substantiate the charge that the said transactions were non genuine and in the nature of funding transactions.
- 3.5 In respect of the transactions executed on January 9, 2001 the Broker stated that it had executed the respective orders of its clients on the online trading terminals of CSE. The Broker had also contended that its client, Maya Trade Links Ltd. was neither its shareholders nor there were any common directors and was not a group company of a broker in any manner whatsoever. The Broker further stated the said Maya Tradelinks Ltd. was holding only 0.45% in SMIFS Capital Markets Ltd. which was a group company holding 49.75% of the paid up equity capital of the Broker. In respect of the transactions executed on January 9, 2001 the Broker claimed that it was wrong to state that the said transactions did not result in any change of beneficial ownership.
- 3.6 In respect of the transactions done by the Broker on February 13, 2001, it had stated that there was no manipulative intent in his transactions and that it had not synchronized the trades deliberately. It claimed that the said transactions were executed through the stock exchange trading system. It has been urged that the Enquiry Officer has accepted the replies in respect of all the allegations made in show cause notice dated November 28, 2003. The Broker has also clarified that the

Enquiry Officer had agreed to their explanations and submissions and accepted that the transactions executed by it on December 21, 2000 and January 09, 2001 could not be considered as non-genuine transactions or funding transactions.

- 3.7 The Broker further claimed that the Enquiry Officer had agreed that there was no material on record to show any linkage in respect of the transactions on February 13, 2001 between it and Biyani Group except the fact that DSQ group companies were the common clients. The Broker further submitted that there were no findings in the investigation report to substantiate the charge that the said transactions were non-genuine and funding transactions.
- 3.8 The Broker contended that there was no manipulative intent in its transactions and that it had not synchronized the trades deliberately and had rather executed them through the stock exchange trading system. In respect of its transactions on March 01, 2001, the Broker submitted that its clients, Hulda wanted to sell 150000 shares and another client Maya Trade Links Ltd. wanted to buy shares of DSQ Industries Ltd. Further it is clarified that the said orders were placed on the trading terminals of CSE. The Broker also submitted that even a warning as recommended by Enquiry Officer would result in severe harm and prejudice since the same would imply a finding of guilt on its part.
- 3.9 The Broker was also granted an opportunity of hearing before SEBI on September 13, 2006. Shri Pesi Modi Advocate represented the Broker and made submissions on behalf of the Broker on the lines of the replies filed by the Broker as stated above. Shri Joby Mathew, Advocate, Shri Santosh Dadheech, Whole Time Director of the Broker and Shri Manish Ajmera, Vice President and Company Secretary of the Broker were also present during the time of the hearing.

4.0 CONSIDERATION OF ISSUES AND FINDINGS

- 4.1 I have perused the investigation report, the Enquiry Report, aforesaid show cause notices dated July 30, 2004, January 27, 2005, the replies of the Broker dated August 18, 2004 and February 04, 2005, the oral submissions made on behalf of the Broker at the time of the hearing and other materials available on record.
- 4.2 The Broker has not disputed the cross deals executed by it for 4,48,000 shares of DSQ on December 21, 2000 on behalf of its clients, Hulda, SMIFS Capital Markets Ltd. (promoter company of the Broker) and Dhanavaridhi Concerns Ltd. In the above cross deals, the selling client was Hulda and the buying clients were SMIFS Capital Markets Ltd. and Dhanbridhi Concerns Ltd. I note that the aforesaid cross deals of the Broker had accounted for 41.18% of the total volume in the said shares at CSE, which was executed at a rate more than 8% of the last traded price. However, the Enquiry Officer found that sufficient evidence has not been adduced to prove that the said transactions were non genuine and executed for the purpose of funding. The Broker contended that the aforesaid transaction was executed as per the instructions of the respective clients. It had clarified that Hulda wanted to sell 4,48,000 shares of DSQ while SMIFS Capital Markets Ltd. and Dhanavaridhi Concerns Ltd. wanted to buy 4,36,000 and 12,000 shares of DSQ respectively.
- 4.3 The Broker further stated that Hulda had delivered only 62000 shares of DSQ against their sale obligation for 4,48,000 shares and that the said client vide letter dated December 23, 2000 informed SMIFS Capital Markets Ltd. that it was unable to deliver the balance 3,86,000 shares of DSQ. Out of the 62,000 shares of DSQ delivered by the said Hulda, the Broker had delivered 12,000 shares to the aforesaid Dhanavaridhi Concerns Ltd. and 50,000 shares to SMIFS Capital Markets Ltd. I note from the said submission of the Broker that SMIFS Capital Markets Ltd. had given its consent to square off the purchase transaction for the balance 3,86,000 shares at the purchase rate itself. The said transaction created volume without delivery.
- 4.4 In the first instance, it is a cross deal wherein the Broker was present on both the sides, by which the anonymity of the trading system was breached, crediting the Broker with the necessary knowledge as to the true purport of the transaction. Further the cross deal resulted in pushing up the price by 8% and thereby impacting the price and volume (by 41.10%). Definitely, these artificial developments generated investor interest. Further, in addition, the fact that SMIFS Capital Markets Ltd. (promoter of the Broking company) had given its consent to square off the purchase transaction for the balance 3,86,000 deliverable to SMIFS Capital Markets Ltd. at purchase rate itself instead of close-out the short delivery as per SEBI's Circular dated December 09, 1996 and thereby foregoing around Rs.2.62 crores as auction proceeds profit being 20% more than the closing price is clearly an accommodation, thereby establishing a strong community of interlacing interest of the Broker and the promoter companies in the cross deals relating to DSQ.
- 4.5 Definitely it is a clear case of accommodation having congruence of interest and such an act could not be anything but compatible with a scheme of manipulation, to which the Broker is a privy.

- 4.6 As regards the transactions executed on January 9, 2001, I note that the Broker upon instructions from his clients SMIFS Capital Markets Ltd. (50,000 shares) and Dhanavaridhi Concerns Ltd. (12,000 shares) executed sale transactions wherein the buyer was Maya Trade Links Ltd. (62000 shares). I observe that the total volume in the shares of DSQ on the said date was 2,62,000 shares. The aforesaid cross deal was executed by the Broker at the rate of Rs.450/- per share as against the market rate of Rs. 339/- per share on December 21, 2000 when it was purchased by the Broker for SMIFS Capital Markets Ltd. and Dhanavaridhi Concerns Ltd. in a cross deal from Hulda. I note that the member client agreement executed by the Broker (in respect of SMIFS Capital Markets Ltd.) was signed by one Shri Deepak Shah. I observe that the said Shri Deepak Shah was also the authorized signatory for the bank account with Indusind Bank of the aforesaid Maya Trade Links Ltd.
- 4.7 In the circumstances, it becomes increasingly evident that the subsequent cross deal on January 9, 2001 involving the Broker among entities who are interconnected as brought out supra were yet another step in manipulating the volume and price of an otherwise illiquid scrip. What is more important, the Broker being present on both sides earlier on December 21, 2000 and later on January 9, 2001 in conspicuous cross deals has been actively associated with the entire gamut of transactions besides having knowledge of the same by virtue of the inter connection established as above.
- 4.8 I also note that the transactions (3,25,000 shares) executed by the Broker on February 13, 2001 accounted for the total volume in the shares of DSQ at CSE. The client of the Broker was Hulda (seller) while the buying brokers were Harish Chandra Biyani (1,70,000 shares) and Biyani securities Pvt. Ltd.(1,55,000 shares). The said transactions were executed in a synchronized manner, being the only transaction in the market on that day. I note that the securities pay-in was made by DSQ Holdings instead of Hulda and that the Broker had delivered the said shares into the beneficiary account of one Shri. Harish Biyani. The Broker stated that Hulda had delivered shares into its pool account and that thereafter on execution of trades, the shares were immediately delivered on the same day to the clearing house of CSE towards early pay-in to ensure proper compliance of the margin. In this connection, I note that CSE vide notice dated January 15, 2001 had informed its members that the trading and settlement of shares of DSQ would only be for trade-for-trade settlement with effect from settlement no. 2001143 till further notice.
- 4.9 The events that transpired on February 13, 2001 as explained by the Broker can be summed up as follows :
- In the transaction under examination Hulda was the seller and the shares were delivered on the same day for early pay-in as claimed by the Broker. But what turned out to be was that the early pay in was adjusted by the Broker against its margin obligation. In this connection, it is pertinent to refer to the notice of CSE dated January 15, 2001 (effective from settlement no.2001143 dated January 19, 2001 until further notice) whereby it is very clear that trading in the shares of DSQ in settlement no. 2001146 would be only for trade for trade settlement of which the Broker was very much aware. As a result of adjustment towards the margin obligation, there was short delivery which was made good by another group entity of DSQ, DSQ Holdings Ltd. Had the DSQ Holdings not given their shares to the delivery obligation of the Broker, the same would have resulted in financial loss to the client. The very fact that the Broker could divert the shares for margin, otherwise meant for delivery despite knowing fully that settlement no.2001146 has to be only by delivery, establishes the violation of the code of conduct. The reason why the Broker did so at the cost of violating the code of conduct is not far to seek, as he was intimately close to the selling group (DSQ) which gave him the comfort of procuring the shares of DSQ at any time. The cross deals and accommodations and various other suspicious features as brought out in this order have to be appraised in the said context. In addition, the Broker, being present on both sides of the transactions was fully aware as to what was really happening in relation to DSQ.
- 4.10 I am satisfied that the Broker was a necessary party to the substantial transaction executed by its clients (some belonging to DSQ), which was only for the purpose of creation of artificial volume and artificial market / price. In view of the above, it is established that the Broker has violated Regulation 4 (a) to (d) of the FUTP Regulations.

5.0 ORDER.

- 5.1 In view of the foregoing, I in exercise of powers conferred vide regulation 13(4) of (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations 2002, hereby impose a major penalty of suspension of the certificate of registration of SMIFS Securities Ltd. (Registration Certificate No. INB030599931), Member, Calcutta Stock Exchange Association Ltd. for a period of six months.
- 5.2 This order shall come into force on the expiry of 21 days from the date of this order.

Place: Mumbai

Date : 15-02-2007

G. ANANTHARAMAN

WHOLE TIME MEMBER

SECURITIES AND EXCHANGE BOARD OF INDIA