

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA

CORAM: G. ANANTHARAMAN.

ORDER

UNDER REGULATION 13(4) SECURITIES AND EXCHANGE BOARD OF INDIA (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002 AGAINST M/S PRASIDDHI MARKETING & SHARE, MEMBER, BANGALORE STOCK EXCHANGE LTD., IN RESPECT OF ITS DEALINGS IN THE SHARES OF HOME TRADE LTD.

WTM/GA/146/ISD/2/07

Date of Hearing: February 15, 2007

Appearances:

For noticee : Shri. Vinay Kumar D.N, Authorized representative

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

1.0 BACKGROUND

- 1.1 The shares of Home Trade Ltd. (hereinafter referred to as HTL) are listed at Pune Stock Exchange Ltd. (hereinafter referred to as PSE) on November 15, 1999 at Rs 250/- and at Bangalore Stock Exchange Ltd. (hereinafter referred to as 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 the share price reached Rs.315/- within two weeks of its listing, i.e. by December 06, 1999.
- 1.2 The subsequent rise in the price of the shares of HTL is as detailed below:

1.3	The maximum rise in the price of the shares of HTL took place between	Date	Price (Rs.)
		December 30, 1999	525.00
		January 31, 2000	735.00
		March 31, 2000	809.00
		April 10, 2000	825.25

November 16, 1999 and March 31, 2000, when it moved from Rs.275/- to Rs.815/-.

- 1.4 In view of the unusual price movement noticed as mentioned above, Securities and Exchange Board of India (hereinafter referred to as SEBI) conducted an investigation into the possible market manipulation/ irregularities in the trading in the shares of HTL to look into the possible violation of 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 FUTP Regulations) and Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Regulations, 1992 (hereinafter referred to as the Broker Regulations).
- 1.5 The investigation conducted by SEBI found that M/s Prasiddhi Marketing & Share (hereinafter referred to as the Broker), Member, BgSE and registered with SEBI as a stock broker had traded substantially in the shares of HTL at BgSE.
- 1.6 The transaction details of the Broker on behalf of his sole client, Shri Chhatar Mal Dugar, in the shares of HTL at BgSE are as follows:

Period	Buy (shares)	% of buy to total volume at BgSE	Sell quantity () shares)	% of sell to total volume at BgSE
April 01, 2001 to December 31, 2001	37,850	13.00%	37,950	13.03%

- 1.7 It has been alleged that the Broker along with other members of BgSE contributed more than 98% of the volumes in the shares of HTL and that the Broker had resorted to circular trading with members of BgSE wherein the shares of HTL were traded amongst themselves and thereby created artificial volumes. In view of the above, it has been alleged that the Broker had violated the provisions of regulation 4(b) of the FUTP Regulations, the provisions of Clauses A(3) and B(2) of the Code of Conduct specified in Schedule II read with regulation 7 of the Broker Regulations, SEBI Circulars dated February 11, 1997 and April 11, 1997.

2.0 APPOINTMENT OF ENQUIRY OFFICER

- 2.1 On completion of investigations, SEBI appointed an Enquiry officer vide order dated May 28, 2003 under regulation 5(1) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as the Enquiry Regulations) to enquire into the alleged irregular transactions of the Broker in the scrip of HTL.
- 2.2 A show cause notice was issued to the Broker in which the following violations were alleged against it.
- "1) There is no introduction of the client. The details regarding the name of the introducer and address in the client introduction form is left blank which is in violation of SEBI Circular No. SMD/POLICY/CIRCULAR/5-97 dated 11.04.1997.
 2. The client was not known to the broker and the orders were placed by Shri Raj Singhi on client's behalf . It is alleged that the member had not met the client and accepted the orders from third party i.e Shri Raj Singhi. It is, therefore, alleged that the member had not exercised due care and diligence while trading in the scrip of HTL. This is in violation of Clause A(2) of the Code of Conduct as specified in Schedule II read with Regulation 7 of SEBI (SB&SB) Regulations, 1992 and SEBI Circular No. SMD/POLICY/IECG/1-97 dated 11.02.97.
 3. It is alleged that the broker had not entered into member client agreement with his client which is in violation of SEBI Circular No. SMD/POLICY/CIRCULAR/5-97 dated 11-04-1997.
 4. It is alleged that the broker had actively traded in the scrip of HTL and resorted to circular trading with other members of BgSE wherein the shares were traded amongst themselves by trades which were not genuine and created artificial volumes. It is, therefore, alleged that the broker had contravened provisions of the Regulation 4(b) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995 and violated Clause A(3) of the Code of Conduct as specified in Schedule II read with Regulation 7 of SEBI (SB&SB) Regulations 1992.
 5. Contract notes were sent to Shri Raj Singhi instead of the client Shri Chhatar Mal Dugar which is in violation of Clause B(2) of the Code of Conduct as specified in Schedule II read with Regulation 7 of SEBI (SB&SB) Regulations, 1992".
- 2.3 The Broker filed its reply and had also made submissions before the Enquiry Officer. The Enquiry Officer vide report dated November 08, 2004 recommended to impose a penalty of censure against the Broker. The Enquiry Officer had inter alia observed that the Broker did not enter into the member client agreement in respect of its client who had traded in significant volumes only in the shares of HTL and thereby, violated the SEBI circular dated April 11, 1997. The Enquiry Officer further observed that there was no introducer in the Know Your Client form and that there was no material to suggest that the Broker had assessed the financial capabilities of the client before permitting him to trade in significant volumes.

3.0 CONSIDERATION OF ISSUES AND FINDINGS

- 3.1 Pursuant to the Enquiry Report, a notice dated November 22, 2004 was issued to the Broker under regulation 13(2) of the Enquiry Regulations asking it 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. The said show cause notice was served on the Broker through BgSE. Sufficient time was given to the Broker to submit its reply to the said show cause notice. However, the Broker had failed to submit any reply.
- 3.2 I have perused the investigation report, Enquiry Report, show cause notice issued to the Broker and other relevant materials available on record. Admittedly, the Broker had not entered into the member client agreement with its client and there was no introducer in the Know Your Client (client registration) form. In view of the above, I am of the prima facie view that the violations committed by the Broker call for a higher penalty than that recommended by the Enquiry Officer. Accordingly, a notice dated September 27, 2006 was issued by SEBI to the Broker asking it to show cause as to why a penalty of suspension of certificate of registration for a period of fifteen days should not be imposed upon it. The Broker vide letter dated October 13, 2006 stated that, even a suspension for a day would create a big damage to all his investor clients. The Broker further requested SEBI to excuse it in the matter and to allow it to trade for its clients without interruption. The Broker vide letter dated October 18, 2006 further stated that it was not involved in the manipulation in the shares of HTL and that it was not involved in any circular trading. The Broker further clarified that client approached it and the orders were placed by the said client. The Broker contended that it had not violated the Rules and Regulations of SEBI.
- 3.3 An opportunity of hearing was also granted to the Broker on February 15, 2007. The said hearing was attended by Shri. Vinay Kumar D.N, as authorized by the Broker and made submissions on behalf of the Broker. He submitted that the client of the Broker who belonged to Kolkata came on his own to the office of the Broker at Bangalore and introduced himself and the orders were placed by the said client over phone from time to time. He admitted that that no member client agreement was executed by the Broker with the said client due to oversight. He also clarified that the Broker had collected margin and there was no delivery of shares. He claimed that the Broker had traded only for five months (July- December) in the year 2001.

- 3.4 I have perused the investigation report, the Enquiry Report, the show cause notices dated November 22, 2004 and September 27, 2006, the letters dated October 13, 2006 and October 18, 2006 sent by the Broker, the oral submissions made on behalf of the Broker at the time of the hearing and other 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.
- 3.5 The fact that the Broker had traded substantially in the shares of HTL on behalf of his sole client (in respect of its transactions in the shares of HTL), Shri Chhatar Mal Dugar has not been disputed. One of the allegations leveled against the Broker is that it had not entered into the member client agreement with its aforesaid client before executing transactions in the shares of HTL. In terms of SEBI Circular dated April 11, 1997, SEBI had framed a uniform format of the client registration form and the member client agreement separately as specified therein. Admittedly, the Broker had not entered into the member client agreement, which according to him was due to oversight. The said explanation of the Broker can not be accepted, as being a market intermediary, the Broker is expected to comply with the regulatory circulars/guidelines which are meant for the protection of the interest of the investors and the securities market in general. The Broker failed to comply with the aforesaid circular of SEBI as expected from a prudent stock broker who had a duty not only towards its client but also towards the securities market. In this context, I note that the client was new to the Broker at the time of the execution of transactions in the shares of HTL and admittedly, the orders were placed by him over phone from Kolkata. The Broker should not have executed trades on behalf of such an outstation client without complying with the basic requirements stipulated by SEBI. In view of the above, by not entering into the member client agreement with its client, I hold that the Broker had violated the above mentioned SEBI Circular dated April 11, 1997 while trading in the shares of HTL.
- 3.6 I note that the trades in the shares of HTL were made by the Broker for a new client, as pointed out above. Though the Broker had executed the client registration form (Know Your Client), I note that the details regarding the introducer was not filled in the said form as stipulated by SEBI vide circulars dated February 11, 1997 and April 1997. The Broker clarified that as the client himself had approached the Broker and expressed his willingness to trade in the shares of HTL, no introduction was taken. The Broker claimed that the signature of its client was attested by the Branch Manager, Punjab & Sind Bank, Sowrangee Lane Branch. However, the Broker had not made any further verification about the genuineness of the said claim. The Broker should have collected the identity/residence proof of its client before executing trades on behalf of him, especially when the client (trading through the Broker for the first time) belonged to a far away place. The very purpose of client registration form is to provide various details of the clients so as to enable the stock broker to evaluate the client before the stock broker takes up trading for him. Above all, the client was new to the Broker and also did not belong to the place of business of the Broker. Therefore, it is fairly established that the Broker had violated the Circulars dated February 11, 1997 and April 11, 1997 by not incorporating the details regarding the introducer in respect of its client.
- 3.7 Further, a stock broker has to verify the financial capacity of his clients before executing trades on their behalf. Such assessment of financial capacity of the client is necessary in order to avoid the risk. When a stock broker fails to perform the above primary requirements and if he is transacting on behalf of such unknown clients without knowing their details and financial capacity, he is putting the entire system in jeopardy. In the present matter, the Broker could not produce any material to suggest that it had assessed the financial capacity of its client before executing trades on behalf of the said client in the shares of HTL, substantially. The Enquiry Officer in his report had mentioned that the Broker had not obtained any financial statements of the client. In the facts and circumstances of the case, by executing trades for a new client without entering into the member client agreement and without any introducer, it is fairly established that the Broker had failed to exercise due skill, care and diligence in the conduct of its business while executing trades on behalf of its client.
- 3.8 I also note that the Broker had failed to submit 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 its client. Despite of executing large transactions, the Broker had failed to obtain the acknowledgement copy of contract notes in respect of the trades executed by it on behalf of its client.
- 3.9 In the facts and circumstances it is established that the Broker had violated Clause A(2) of the Code of Conduct prescribed under Schedule II of the Broker Regulations and the circulars of SEBI dated February 11, 1997 and April 11, 1997. The aforesaid violations committed by the Broker cannot be taken lightly and the same call for a higher penalty than that recommended 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 Prasiddhi Marketing & Share (INB081117310), Member, Bangalore Stock Exchange, Ltd. for a period of fifteen days.

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

G. ANANTHARAMAN

WHOLE TIME MEMBER

SECURITIES AND EXCHANGE BOARD OF INDIA

Place: Mumbai

Date : 22-02-2007