

SECURITIES AND EXCHANGE BOARD OF INDIA

Dr. T. C. NAIR, WHOLE TIME MEMBER

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ORDER

UNDER REGULATION 13(4) OF SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002, AGAINST M/s. LALKAR SECURITIES PRIVATE LIMITED, MEMBER, BOMBAY STOCK EXCHANGE LIMITED (SEBI REGISTRATION NO. INB 010991133) IN THE MATTER OF M/S. SPANCO TELESYSTEMS AND SOLUTIONS LIMITED

WTM/TCN/ID3/89/02/2007

BACKGROUND

1. Spanco Telesystems and Solutions Limited (hereinafter referred to as "STSL") promoted by Shri Ashok Oberoi, Shri Bansilal Tandon, Shri V V Balakrishnan, Shri Vinod Kumar Nemani and Shri Jai Prakash Nemani was originally incorporated in 1984 as Kadambari Leasing Private Limited. Kadambari Leasing Private Limited had taken over business of STSL and adopted its name with effect from November 11 1999. In 1984, the company had come out with a public issue of 1, 50, 000 shares at par and was listed on the Bombay Stock Exchange Limited (hereinafter referred to as "BSE").
2. Securities and Exchange Board of India (hereinafter referred to as "SEBI") received certain complaints about price rigging in the scrip of STSL. After receiving the observations relating to the same from BSE, SEBI conducted an investigation into the affairs of STSL for the period from October 1, 2000 to July 31, 2001 (hereinafter referred to as "investigating period"). The observations under the investigation are as under:
3. In an Extra Ordinary General Meeting held on December 11, 1999, STSL passed a resolution to allot 10,00,000 shares to its promoters and transfer its management control to Kapil Puri Group. The same day 10,00,000 preferential shares at Rs.10/- each were issued to Kapil Puri Group and others comprising individuals, not necessarily shareholders of STSL. The shares were listed on BSE on February 24, 2000. As on October 10, 2000, Shri Kapil Puri was Chairman of STSL.
4. From the distribution schedule of STSL as on August 24, 2001, it was observed that the public holding in STSL was only 5, 77, 000 equity shares amounting to 8.26%. FIIs, NRIs, and Banks together had a holding of less than 1%. Other Body Corporates held 29.80%, while Promoters of STSL held 61%. Out of 637 shareholders, 19 shareholders held 94.67% of the equity capital of STSL.
5. A preferential allotment of 22,50,000 shares at Rs.15/- each (premium Rs.5/-) was made under section 81(1A) of the Indian Companies Act, 1956, on 16.02.00, to the parties as mentioned in the table below. These shares were listed on BSE on June 26, 2000.

S.No.	Name of the Allottee	Shares Allotted
1	Shri Kapil Puri	8,00,000
2	Neha Equisearch Pvt Ltd	3,75,000
3	Smt Kavita Puri	2,55,000
4	Shri Rajesh Chhabria	2,30,000

5	Shri Mahendra G Shah	2,00,000
6	Shri Sanjeev Chainani	1,75,000
7	Shri Kishore Saigal	60,000
8	M/s Networth Stock Broking Ltd	50,000
9	Smt Chanderkanta Malik	50,000
10	Sarvpriya Leasing Pvt Ltd	20,000
11	Shri Sudanshu Tewari	20,000
12	Shri Naresh Bahri	15,000
	Total	22,50,000

6. Further, a special resolution was passed in an Extra Ordinary General Body Meeting convened on 30.01.01 under section 81(1A) of Companies Act, 1956 to allot 30,00,000 equity shares at Rs.52/- each (premium Rs.42/-) on preferential basis to the following persons:

S.No.	Name	Shares Allotted
1	Shyam Telecom Ltd	15,60,000
2	Shri Rajesh Chhabria	7,20,000
3	Shri Kapil Puri	7,20,000
	Total	30,00,000

7. Though the resolution was passed to allot shares in the above manner, no allotment was made within stipulated period of three months. An Extra Ordinary General Meeting was held on May 29, 2001 wherein a resolution was passed to allot 30,00,000 shares at Rs.10/- each for cash at a premium of Rs.27/- per share aggregating to Rs.11,10,00,000/- on preferential basis to the persons mentioned in the above table. It was observed that this premium structure was reduced from Rs.42/- to Rs. 27/- per share.
8. It was observed that there was an effort to create artificial volume in the scrip of STSL during the period of investigation, to influence the terms and conditions of the preferential allotment mentioned hereinabove. It was alleged that a set of brokers/members of BSE have traded in the scrip of STSL and indulged in creating artificial volumes thereby influencing the price of the said scrip. Accordingly, it is alleged that volumes in the scrip of STSL were high as compared to the volumes prior to and after investigation period. The price of the scrip on October 1, 2000 was Rs.50/- with a volume of 1,000 shares. The price had reached its peak of Rs.54.95/- on October 06, 2000 and the number of shares traded were 2,300 after which the price had come down to a low of Rs.18.80 with 14, 660 shares being traded on April 20, 2001. Further, it was noticed that the price of the scrip had started rising and by June 29, 2001; it had reached Rs. 44.55/- with a trade volume of 61,460 shares. After this period, the price of the scrip again started falling and at the end of the investigation period i.e., on July 31, 2001, the price of the scrip was hovering around Rs. 26/- whereas traded volume reported at the exchange on the same day was 7,600 shares.
9. Investigations revealed that M/s. Lalkar Securities Pvt. Ltd. (hereinafter referred to as LSPL or the broker), had traded in the scrip of STSL for its clients Shri S Shaktisaravanan, Shri Manivanan and M/s. Raj Investments. In performing these transactions, the broker was found to have failed to exercise due care and skill in his dealings thereby violating the provisions of Clause A (2) of the Code of Conduct mentioned in Schedule II read with Regulation 7 of SEBI (Stock Broker and Sub-broker) Regulations, 1992. It was also alleged that the broker had not collected margin money from clients violating the provisions of SEBI Circulars SMD/SED/CIR/93/23321 dated November 18, 1993, SMDRP/POLICY/CIR-35/98 dated December 04, 1998, SMDRP/POLICY/CIR-7/99 dated February 4,2000 and SMDRP/POLICY/CIR-33/2000 dated July 27, 2000.
10. In view of the aforesaid findings of investigation, an enquiry was recommended against the sub-broker.

ENQUIRY REPORT, FINDINGS AND RECOMMENDATIONS

11. An Enquiry Officer was appointed by SEBI vide its order dated October 13, 2003 to inquire into the aforesaid allegations against the broker. The Enquiry Officer after conducting the inquiry, following the due procedure laid down in this regard, had submitted his report to the Board on 01.06.05. Vide the said report, the Enquiry Officer found the broker had not acted in good faith and that it failed to exercise due skill and care. By virtue of this, the broker's conduct was found not to be in conformity with the Code of Conduct prescribed in Schedule II of SEBI (Stock Broker and Sub-broker) Regulations, 1992. In view of the aforesaid findings, the Enquiry Officer recommended a minor penalty of censure, to be levied on the broker.

SHOW CAUSE NOTICE AND REPLY

12. The Board, after considering the recommendations of the enquiry officer, issued a show cause notice dated June 13, 2005 to the broker, enclosing a copy of the enquiry report, requiring the broker to show cause as to why appropriate penalty including penalty as recommended by the Enquiry Officer should not be imposed on it. It was also mentioned that if the broker failed to reply within 15 days of the receipt of the notice, then it would be presumed that the broker had no explanation to offer and the Board shall be free to take such action as it deems fit. The broker had replied vide its letter dated July 15, 2005. The important submissions of the broker are as under -

- Nowhere in the entire order was the Enquiry Officer was able to prove that the said trades carried out by their clients were artificial in nature or which were entered to create false appearance of trading in the market
- Nowhere the Enquiry Officer had raised any doubts about the genuineness of the clients or propriety of the trades done for the clients as regards the financial capability of the client
- As regards the allegation that in the case of Shri S. Manivannan where the occupation has been shown as investor, the client has given details of his residence from where he used to operate and therefore there is no reason to raise doubt about the genuineness of the client
- The Enquiry Officer has exceeded his authority since no where in the notice has any doubt been raised or any allegation made about the financial capability of the clients
- In case of Shri S. Shakti Sarvanan, the client has given his residential address and therefore, the question of giving office address does not arise
- Nonfilling of columns like telephone number, market value of portfolio are purely lapses of a technical and venial nature and can in no way be termed as deficiency in knowing the financial health/ capability of the client
- The Enquiry Officer has admitted that the so called persons who were acting in concert with the management had indulged in price manipulation and offered the shares instead to the public in preferential allotment
- The non filling of certain columns in the KYC form are not of much significance and the Enquiry Officer has tried to make out the case in finding mistakes for which no case can be made out
- The appreciation of evidence is totally and grossly misconstrued
- The learned Enquiry Officer has based his presumption on the ground that the noticee has not practiced due care, skill and diligence since the trades of the clients have resulted mostly in squaring
- The whole exercise done by the Enquiry Officer is to find the noticee in the wrong path, whereas, there is no evidence of any violation of Code of Conduct or to make an order against the noticee.
- The learned Enquiry Officer has not brought out any specific violation or contravention of rules and regulations
- They were not involved nor indulged in any act that has been detrimental to the investors' interest or which lead to interference of the fair and smooth functioning of the market
- All orders were executed in accordance with generally accepted principles and had been faithful in executing the trades at the best available market prices with contract notes issued as per requirements
- They have always adhered to comply with the rules and regulations of the SEBI Act and the regulatory provisions both in letter and in spirit and that the noticee should be discharged
- That the only income earned by the noticee is the lawful brokerage earned out of transactions.

In view of the aforesaid submissions, the noticee requested that the penalty of censure as recommended by the Enquiry Officer should not be imposed.

CONSIDERATION OF ISSUES

13. I have taken note of the findings of the investigation against the broker. I have also perused the Enquiry report, the findings arrived at and the reply dated July 15, 2005 sent by the broker in response to the Show Cause Notice. Since the penalty recommended by the Enquiry Officer is only 'censure' I feel that no hearing is required in the matter and I proceed to consider the issues:

- i) Whether the broker failed to exercise the due care and diligence as expected in terms of the provisions of the Code of Conduct as specified in Schedule II read with Regulation 7 of SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992
- ii) Whether the broker failed to collect margin money from its clients for the aforesaid trades thereby violating the SEBI Circulars SMD/SED/CIR/93/23321 dated November 18, 1993, SMDRP/POLICY/CIR-35/98 dated December 04, 1998, SMDRP/POLICY/CIR-07/99 dated February 4, 2000 and SMDRP/POLICY/CIR-33/2000 dated July 27, 2000.

14. From the findings in the Enquiry Report, I note that the broker had not obtained the necessary information of two of their clients, Shri S Manivanan and Shri Shakti Saravanan, who are based in Trichy and Chennai, respectively. I note that the broker had not obtained the telephone number and occupation (in the occupation column in the KYC it is mentioned as 'investor') of Shri S Manivanan. The Permanent Account Number (PAN) and the Annual Income for the preceding three years have also not been obtained from their client. For Shri Shakti Saravanan, it was found that his 'Know Your Client Form' did not contain proper details and market value of his portfolio was also not mentioned while he had become the client of the broker on December 12, 2000.

15. The broker submitted vide its reply dated July 15, 2005 that the above said lapses were 'technical and venial' in nature. Such details are important to know all particulars about their clients and their status in the capital market. I therefore, reject the contention of the broker that certain columns are of not much significance. In this connection, I strongly opine that the particulars in the Know Your Client Forms are of much importance and are prescribed only to elicit true and correct information about the clients and to ensure that unscrupulous people are filtered at an early stage. Clause A of Schedule II of the SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992 which deals with the general conduct of a Stock Broker reads as under:

"A. GENERAL

(1) Integrity: A stock-broker, shall maintain high standards of integrity, promptitude and fairness in the conduct of all his business.

(2) Exercise Of Due Skill And Care: A stock-broker, shall act with due skill, care and diligence in the conduct of all his business.

(3) Manipulation: A stock-broker shall not indulge in manipulative, fraudulent or deceptive transactions or schemes or spread rumours with a view to distorting market equilibrium or making personal gains.

(4) Malpractices: A stock-broker shall not create false market either singly or in concert with others or indulge in any act detrimental to the investors interest or which leads to interference with the fair and smooth functioning of the market. A stock-broker shall not involve himself in excessive speculative business in the market beyond reasonable levels not commensurate with his financial soundness.

(5) Compliance With Statutory Requirements: A stock-broker shall abide by all the provisions of the Act and the rules, regulations issued by the Government, the Board and the stock exchange from time to time as may be applicable to him. "

Thus a broker should exercise due care and diligence which is a duty cast on brokers while trading in securities. Since the broker has failed to obtain full and proper information from his clients in their 'Know Your Client Forms', they have contravened the provisions of Clause A(2) of Schedule II of the SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992. I find that a penalty of censure would however, be commensurate with the gravity of the aforesaid violations.

16. The other charge against the broker is that they have failed to collect the margin money for the trades, which is in violation of SEBI Circulars SMD/SED/CIR/93/23321 dated November 18, 1993, SMDRP/POLICY/CIR-35/98 dated December 04, 1998,

SMDRP/POLICY/CIR-07/99 dated February 04, 2000 and SMDRP/POLICY/CIR-33/2000 dated July 27, 2000. With regard to this charge, I note that the broker has submitted that no margin is required to be collected after applying the threshold limit of Rs.1 lakh in terms of SEBI Circular dated February 04, 2000. The said circular prescribes that where the margin in respect of a client in a settlement work out to more than Rs.1,00,000/-, then the brokers would have to mandatorily collect the same from the client. The Enquiry Officer has observed in his report that the broker had explained that with respect to each of their client no margin money needed to be collected mandatorily. Moreover in this regard the Enquiry Officer had accepted the submission of the broker and did not find any contravention of the provisions of the above said circulars. Hence the said allegation cannot stand against the broker.

ORDER

17. In view of the above, I, in exercise of powers conferred upon me by virtue of Section 19 of the Securities and Exchange Board of India Act, 1992 and Regulation 13 (4) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002, direct that a penalty of censure be imposed on M/s. Lalkar Securities Private Limited (SEBI Registration No. INB010991133), member of Bombay Stock Exchange Limited.

Date: 22.2.2007

Place: Mumbai

T C Nair
Whole Time Member
Securities and Exchange Board of India