

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA

CORAM: V. K. CHOPRA, WHOLE TIME MEMBER

Against M/s Active Finstock Pvt. Ltd., Broker, Bombay Stock Exchange Ltd. (BSE) in the scrip of Mazda Fabrics and Processors Ltd.

DATE OF HEARING: 08.12.2006

APPEARANCES:

FOR COMPANIES/ BROKERS:

1. Shri. P. N. Modi, Counsel
2. Shri. R. R. Bhansal, Advocate
3. Shri. V. Khandwala, Director, Active Finstock Pvt. Ltd.

FOR SEBI:

1. Mrs. Barnali Mukherjee, DGM, SEBI
2. Shri. Deepesh M. U., Manager, SEBI
3. Shri. Mohamed Rahaz P.M., Legal Officer, SEBI

ORDER

{Under Regulation 13(4) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002}

1.0 BACKGROUND

- 1.1 Securities and Exchange Board of India (hereinafter referred to in short as "SEBI") conducted investigation into the market manipulation in the scrip of M/s Mazda Fabrics and Processors Ltd. (hereinafter referred to as "MFPL"). The trading details of various entities who traded in the scrip of MFPL were collected. The data and volumes contributed by these entities including M/s Active Finstock Pvt. Ltd. (hereinafter referred to as "Noticee"), a registered broker of the Bombay Stock Exchange Ltd. (BSE) with SEBI registration no. INB 010849331, were analyzed.
- 1.2 The investigations revealed that the Noticee had actively traded in the scrip of MFPL at BSE on behalf of their major clients M/s Chirag Investments (hereinafter referred to as 'Chirag') and M/s Khandwala Finstock during the period of investigations i.e. May 29, 1996 to August 30, 1996 and contributed to the creation of liquidity / volumes in the scrip of MFPL.
- 1.3 After considering the Investigation Report, SEBI appointed an Enquiry Officer to enquire into the affairs and dealings of the Noticee for finding out the possible violations of the provisions of Securities and Exchange Board of India Act, 1992 (hereinafter referred to as "SEBI Act"), 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") and Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Regulations, 1992 (hereinafter referred to as "Stock Brokers Regulations").
- 1.4 The Enquiry Officer, after conducting an enquiry in accordance with the provisions 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'), submitted a report dated January 04, 2006. The report revealed that Noticee has violated the provisions of Regulation 7 read with Code of Conduct as specified in Schedule II of Stock Brokers Regulations and Regulation 4(a) to (e) of PFUTP Regulations. The Enquiry Officer recommended suspension of registration of the Noticee for a period of one month.

2.0 SHOW CAUSE NOTICE

- 2.1 Pursuant to the receipt of the Enquiry Report, a Show Cause Notice dated January 25, 2006 enclosing therewith a copy of report was issued to the Noticee advising it to show cause as to why action as recommended by the Enquiry Officer or penalty as considered appropriate should not be imposed on it. The Noticee submitted its reply to the said show cause notice, vide letter dated April 04, 2006.

3.0 REPLY OF THE NOTICEE

- 3.1 The Noticee did not accept or admit anything stated in the Notice and submitted as under:
 - 3.1.1 That they had no connection or nexus either with the company, MFPL or its promoters.

- 3.1.2 That they had traded on behalf of Chirag in ordinary course of business and the said trades were executed between the price band of Rs 14/- to Rs 42/- which constituted mere 2.4% and 2% of the buy and sell volume respectively during May 29, 1996 and August 30, 1996. They have also stated that they had no links or nexus with brokers viz. Bhagwadas Bhogilal, Saurashtra Capital and S V Shah etc. who had traded in the scrip at the relevant time. Regarding the trading carried out by them on behalf of Khandwala Finstock, they submitted that the said fact was not there in the show cause notice issued prior to the enquiry proceedings and as such Enquiry Officer should not find anything beyond the show cause notice. However, they stated that the trades executed on behalf of Khandwala Finstock were in their ordinary course of business.
- 3.1.3 That they knew Shri. Ashok Bharadia only in his capacity as a Director of Wallfort Financial Services Ltd(hereinafter referred to as "WFSL") and they are not aware whether he was a Director of Clio Finance Ltd (hereinafter referred to as "CFL").
- 3.1.4 That the Enquiry Officer has misinterpreted their statement regarding their awareness of WFSL.
- 3.1.5 That they had no relationship with Chirag except that of a broker client relationship and Chirag was one of the thousand clients they had at the relevant time.
- 3.1.6 That they were not aware that WFSL was involved in managing the public issue of MFPL or in bringing out application to bail out the issue or in financing the issue. They added that they were also not aware that Shri. Anil Jain was placing orders in the scrip of MFPL and that he was choosing the brokers.
- 3.1.7 That Chirag was their client from June 19, 1996 to August 21, 1996. They agreed that an amount of Rs 9,700/- was due as on August 16, 1996 and this amount was passed on to WFSL by a journal voucher.
- 3.1.8 That there is no supporting material to demonstrate that Chirag had opened a trading account with us at the behest of Shri. Anil Jain and it was Shri. Anil Jain who was placing orders with them instead of Chirag. The Noticee further stated that they had traded for Chirag strictly in consonance with its instructions. They used to receive oral instructions from Chirag for the placement of orders and all payments and dealings were made from / to the account of Chirag as per its instructions.
- 3.1.9 That the volume of trades in the scrip of MFPL was insignificant and they have not violated any of the provisions of PFUTP Regulations or Code of Conduct specified under the Stock Brokers Regulation.
- 3.1.10 That at the relevant time they were not aware of any role of WFSL in the bailing out of the public issue.

4.0 HEARING

- 4.1 While submitting reply to show cause notice, the Noticee requested for personal hearing. The Noticee was accordingly advised to attend a personal hearing before me at the Head Office of SEBI at Mumbai on December 8, 2006. Shri. V. Kandwala, Director, Active Finstock Pvt. Ltd., attended the hearing alongwith his advocates Shri. P. N. Modi and Shri. R. R. Bhansal. They requested time to file written submissions which was granted and the same was filed by them on December 19, 2006. In the written statement they by and large reiterated the same submission which they had already made in their reply to the show cause notice. I have considered their reply and written submission while dealing with this matter.

5.0 CONSIDERATION OF ISSUES & FINDINGS

- 5.1 I have carefully examined the findings of investigation, enquiry report, show cause notice, reply of the Noticee and the post hearing written submissions made by the Noticee.
- 5.2 MFPL was incorporated in the year 1994 as a Private Limited Company and it was converted into a Limited company in the year 1995. The certificate of registration of MFPL was obtained on October 5, 1995. The promoters of MFPL were Shri Bharat Kumar Jain and Shri Prakashkumar Jain. It had come out with a public issue in the year 1996 for 36,38,300 shares @ Rs 10/- per share at par. The issue which opened on March 06, 1996 and closed on March 16, 1996 was undersubscribed and the promoters of the MFPL got the public issue bailed out with the help of external financiers viz. Shri. Suresh Bafna and Shri. Anil Jain who were directors of the Co-Lead Manager to the issue i.e CFL as also of the Wallfort group of companies.
- 5.3 The issue opened on March 06, 1996 and closed on March 16, 1996. The net offer to the resident Indian public was for 16,00,000 shares i.e. for Rs 1,60,00,000/-. In terms of prospectus, any unsubscribed portion out of the reservation to OBCs / NRIs / FIIs / MFs / FIs and Banks (which was for 18,56,400 shares of MFPL) was to be added to the net public offer. However, since none of these entities subscribed to the issue, the total offer to the resident Indian public went up to 34,56,400 shares. Clause 6.3.8.1 of the SEBI (DIP) Guidelines prescribes 90% of the shares offered to the public, as the minimum subscription to be received. In the present case, the minimum subscription that was stated to have been received was for 30,92,100 shares i.e. almost 0.90 times (90% being offered to the public being 3110760 shares). From the minutes of the board meeting held on May 10, 1996, it is seen that 31,93,100 shares had been allotted to the public, the

difference being shares allotted to one Shri. Rajesh Chauhan whose allotment application through stock invests was cancelled by the bank manager without reference to the company.

5.4 The equity shares of the company, MFPL were listed on the Stock Exchange Mumbai (BSE) w.e.f. May 29, 1996. The price of MFPL scrip at the time of listing was quoting around Rs 15 to Rs 16, and it touched a high of Rs 112.50 on August 30, 1996 from a low of Rs 8.50 on June 06, 1996.

5.5 I find that the proceeds of the public issue of MFPL were routed through front entities of the promoters of MFPL to repay the financiers with interest. The concerted trading of such front entities had resulted in rise in price and volume in the scrip of MFPL. Investigations revealed that there was rigging of the share price and volumes in MFPL scrip in a short span of time by the front entities who were clients of various brokers.

5.6 I observe from the records that the total volume of trading in this scrip at the exchange during the period May 29, 1996 to August 30, 1996, was 41,43,500 shares. BSE had levied special margins to control every rise in the price of MFPL scrip in the following manner:

Rs.10/- on 13.06.96

Rs.15/- on 18.06.96

Rs.30/- on 24.06.96

Rs.36/- on 22.07.96

Rs.54/- on 29.07.96

Rs. 40/- on 05.08.96

Rs.45/- on 12.08.96

5.7 Further circuit filters were first revised from 25% to 10% on July 2, 1996 and later from 10% to 5% on July 22, 1996. Further, BSE also suspended trading in the scrip of MFPL for one day on August 14, 1996 and subsequently for 3 days from September 2 to September 4, 1996. Later on, SEBI approved indefinite suspension of this scrip from September 9, 1996.

5.8 I find that the top 6 brokers had contributed 53.59% of the total buy volume at the exchange and 49.71% of the total sell volume at the exchange. The Noticee was one of the brokers out of the group of six and had actively traded in the scrip of MFPL at BSE on behalf of their clients Chirag and Khandwala Finstock during the period May 29, 1996 to August 30, 1996. I have also noted from the record that their buy and sell volumes in the shares of MFPL were 2.90% and 2.33% respectively of the total volumes of the Exchange.

5.9 I observe that the Noticee had traded in the shares of MFPL on behalf of their major client Chirag during the settlement nos. 6, 7 and 8 of the year 1996. The position of Noticee vis-à-vis their client was as under:

S.No./dates	Position of Noticee			Position of Chirag		
	Buy	Sell	Net	Buy	Sell	Net
6 (26.5.96-7.6.96)	20,000	20,000	0	20,000	20,000	0
7(9.6.96-21.6.96)	62,500	46,500	16,000	62,500	46,500	16,000
8(24.6.96-5.7.96)	15,700	15,700	0	14,700	14,700	0

5.10 From the above, it is clear that the majority of the position (except for 1000 shares of MFPL in settlement no 8) built by Noticee in the scrip of MFPL was on behalf of their client, Chirag. This apart, Noticee had also transacted in settlement nos. 9, 10 and 11 for Khandwala Finstock, an associated entity of theirs. The Noticee has not denied their association with the client Khandwala Finstock. Instead, they made a passing reference in their reply to the show cause notice that the said fact was not there in the show cause notice issued prior to the enquiry proceedings. However, in the instant proceedings, Noticee admitted these trades and stated that the same were executed on behalf of Khandwala Finstock in the ordinary course of business. The details of the said trades are reproduced in the table below:

Settlement No.	Position of Noticee		
	Buy	Sell	Net
9	1400	1400	0
10	2000	----	2000
11		2000	(Auctioned out)

5.11 From the above details of trade, it is clearly found that the Noticee had mainly executed trades for its client Chirag and Khandwala Finstock and to see their linkage, I have examined the statements of Shri Vimal Khandwala, director of the Noticee and Shri Suresh Bafna, a director CFL, the Co-Lead Manager to the public issue of MFPL, Shri Anil Jain, director of CFL and Wallfort group.

5.12 Statement of Shri Vimal Khandwala, Director of AFPL made on June 27, 2002:

- a. Shri Ashok Bharadia of WFSL introduced Chirag.
 - b. WFSL was their client during the relevant period.
 - c. The trading account of Chirag was operational from June 19, 1996 to August 21, 1996.
 - d. An amount of Rs.9700/- was due on August 19, 1996, which was passed on to WFSL by passing a journal ledger entry.
 - e. Noticee did not have any written authorization from Chirag to transfer the said amount, as WFSL had introduced the client to them.
 - f. The transactions in settlement nos 9 and 10 were auction transactions as the word 'c' appears in the ledger done for Chirag.
- 5.13 Statement of Shri. Suresh Bafna made on May 2, 2002, May 7, 2002, May 15, 2002, May 17, 2002 and 4th June, 2002.
- a. Shri Ashok Bharadia was the director of CFL.
 - b. Shri Anil Jain and Shri Ashok Bharadia handled all the affairs of WFSL and Wallfort Share and Stock Brokers Ltd. (WSSL).
- 5.14 Statements of Shri Anil Jain made on May 13, 2002, May 14, 2002 and June 1, 2002
- a. He was a director of Wallfort group.
 - b. The proprietor of Dhananjay Holdings was Shri Manoj Bharadia who is brother of Shri Ashok Bharadia and Director of WSSL.
 - c. CFL and WFSL had common Directors.
 - d. He was also the Executive Director of CFL while the MD of CFL was Shri Suresh Bafna.
 - e. CFL was a co-lead manager to the public issue of MFPL.
 - f. Suresh Bafna, who accepted to arrange finance for the public issue, knew the promoters of MFPL.
- 5.15 It is clear from the details given above that Chirag, a client of the Noticee had traded extensively through them in MFPL scrip. Chirag was introduced to the Noticee as a client by Shri Ashok Bharadia, Director of CFL and WFSL. WFSL was earlier a client of the Noticee, which establishes the fact that WFSL was well known to the Noticee. CFL were the Co-Lead Manager in the public issue of MFPL. As confirmed by Shri Bharat Kumar Babulal Jain vide his statement dated July 10, 2002, all the matters pertaining to the applications, the requirement of meeting the minimum subscription in order to bail out the public issue of MFPL etc. were handled by WFSL and CFL. In the client opening form of Chirag with Federal Bank Ltd., Fort Branch, Shri Chandan Sharma, is shown as the proprietor of the firm and Shri Anil Jain as the Director of CFL who introduced the said bank account. Shri Sharma was an entity known to Shri Prakash Jain; Joint MD of MFPL.
- 5.16 The client account of Chirag with Noticee was opened on June 19, 1996 and closed on August 21, 1996. WFSL had applied for 5,40,000 shares in the public issue of MFPL through an application arranged by CFL. CFL then arranged 21,60,000 shares i.e. 67.65% out of 31,93,100 shares of MFPL to be allotted to the public, to bail out the issue. As confirmed by Shri Suresh Bafna, the affairs of WFSL were managed by Shri Anil Jain and Shri Ashok Bharadia. Shri Anil Jain was one of the top 10 shareholders of MFPL and was allotted 20,000 shares of MFPL amounting to 0.34% of the equity capital of MFPL. The telephone no of Chirag was shown to be 3712701, which belonged to Shri Prakash Jain, Joint MD of MFPL. However, the Noticee submitted that they were having only broker client relationship with Chirag and there was no link or connection with the promoters/directors of WFSL/MFPL/CFL/WSSL. This is totally contradictory with the statements of the above persons. Further, the nature of trades executed by the Noticee on behalf of its client Chirag strengthen the case that they acted in concert with each other and also acted and executed the pre-determined plans of the entities associated to manipulate the scrip.
- 5.17 From the above, it is clear that both the bank account and trading account of Chirag were introduced to the bank and broker respectively by persons belonging to the Co-Lead Manger to the public issue of MFPL (who were also involved in bailing out of the issue), that too at around the same time when MFPL came out with public issue. The contact telephone number of Chirag actually belonged to Prakash Jain, the Joint MD and Promoter of MFPL which proves that Chirag is closely associated to the promoters of MFPL.
- 5.18 I further find that that Noticee had transferred the credits lying to the account of Chirag to WFSL and V&U, their earlier sub broker, who had actually introduced WFSL. The said fact was also accepted by Vimal Khandwala of Noticee vide his statement dated June 27, 2002 as also the fact that another amount of Rs. 1006.60 which was lying to the credit of Chirag was also transferred to WFSL and Rs.9693.40 to the account of V&U, their sub broker. The Noticee submitted that the same was done on the basis of the oral instructions received from Chirag and no adverse inferences can be drawn against them only because of such transfer of amount. However no proof/ documentary evidence was submitted by Noticee to substantiate this contention. This transfer of amount though minimal, from one account to another i.e. to the accounts of WFSL (who had introduced Chirag) and V&U, their sub broker (who had introduced WFSL) throws light on the relationship between the entities i.e. V&U, WFSL Chirag and Noticee.
- 5.19 While the Noticee had mainly traded for Chirag it had also traded for Khandwala Finstock, one of its associates. The trading for Chirag had commenced in the same settlement when the scrip was introduced for listing i.e. May 29, 1996, while Noticee continued trading for Khandwala Finstock in Settlement nos 9,10 and 11 almost till the time the shares were suspended for trading on September 9, 1996. Although Noticee traded for Chirag only in 3 settlements, they had squared off all the transactions executed for the said client, except for 1,000 shares in settlement No 8. Noticee had also taken a stand before the Enquiry Officer that their relationship with Chirag was only that of a broker-client and that they had no relationship with any of the other brokers, trading in the said scrip or with the company, its promoters or its management.

Further, they have also stated in their reply to the post enquiry show cause notice that squaring off transaction is a well-accepted market practice and they did not find anything amiss in the trading of Chirag.

- 5.20 The said contention of the Noticee is not acceptable as the relationship between the Noticee and other connected entities is established from the details given in the preceding paragraphs. The statements of the various persons referred above clearly indicate that the Noticee was well aware about the nexus/relationship between its client and other connected entities. In fact this may be the reason for non application of necessary due diligence required to be done by a broker, while verifying the bonafides of their client; Chirag. Admittedly no documents were collected by the Noticee in order to verify the bonafides or the financial worthiness of the real client and instead, total reliance was placed upon the introducer of the client. The fact that the introducers of the said client besides being well known to Noticee, were entities associated with issues like management of the public issue of MFPL, financing the issue and bailing out the same, reinforces the finding that all the entities in question; i.e. Noticee, their client and the entities connected to MFPL, had a common objective, borne out of a nexus between them. This nexus is further reinforced by the fact that Chirag traded extensively in one specific scrip, during a specific period in settlement nos. 6, 7 and 8, right from the time of listing of the said scrip in a manner that they were a part of a set of common entities. When Noticee transacted for Chirag, the counter party brokers were taking the opposite position for clients related to Chirag or associated with MFPL. Thus a common set of clients acting in concert through selected brokers were noted to be trading in the scrip of MFPL in a circular manner as evident from the details hereunder: (As given in the next page)

SetNo	Date	Qty. purchased by RFS	Counter party broker	Counter party client	Qty	Qty. sold by RFS	Counter party broker	Counter party client	Qty
6	26.5.96 – 7.6.96	66300	BB & Co.	Sneha	29100	62500	Active	Chirag	15000
			Libord	Subhash	15000		BB & Co.	Sneha	25800
			SVS	Sikha	15000		Libord	Subhash	15000
7	9.6.96-21.6.96	132100	BB & Co.	Sneha	117900	100400	BB & Co.	Sneha	79200
			Libord	Subhash	11000				
8	24.6.96-5.7.96	28700	BB&Co.	Sneha	28800	20700	BB&Co.	Sneha	9700
							Active	Chirag	7200
10	22.7.96-2.8.96	10300	BB & Co.	Sneha	6700	4400	BB & Co.	Sneha	2000
11	5.8.96-16.8.96	7200	BB & Co.	Sneha	4300	1000	BB & Co.	Sneha	1000
12	19.8.96-30.8.96	3000	BB & Co.	Sneha	2800	2300	BB & Co.	Sneha	500

[BB&Co. : Bhagwandas Bhogilal & Co.- Libord : Libord Securities-SVS: SVS Securities Ltd- Active : Active Finstock Sneha:Sneha Invesments-Subhash: Subhash Trading & Co.-Sikha : Shikha Finance- Chirag: Chirag Investments]

- 5.21 I observe that BB&Co, Libord, SVS and Noticee were amongst the top 6 counter brokers, who traded actively in the scrip of MFPL. The proprietors of RFS, Sneha and Subhash namely Rajesh Kumar Parasmal Jain, Hasmukh Parasmal Porwal and Subhash Parasmal Porwal are brothers and Bharatkumar Jain, MD of MFPL is their maternal uncle. The proprietor of Shikha Investments is Parasmal Babulal Jain, the elder brother of Bharat Kumar Jain. All the above-mentioned clients had submitted that they were unaware of the funds movement in the respective bank accounts as also about the secondary market transactions in their names. They stated that they had signed blank account opening forms and cheque books at the insistence of Shri Bharat Jain who was the promoter as well as Managing Director of MFPL. This fact has been corroborated by Bharat Jain in his statement dated July 10, 2002, while admitting that the said blank account opening forms and cheque books were handed over to Shri Anil Jain. Shri Suresh Bafna, Director of CFL or Shri Anil Jain introduced all the accounts. In the account of Chirag, introduced by Shri Anil Jain, Director of CFL (also director in Wallfort group that arranged finances), the phone number was that of Shri Prakash Jain, Joint MD of MFPL. As apparent from the table above, for the trades executed by Noticee for Chirag, Saurashtra Capital Services were the counter party for their client, Rajesh Financial Services, who was one of the major entities trading actively in the scrip of MFPL and found to be close to the promoters of MFPL.
- 5.22 From the above, it is clear that entities connected to the promoters of MFPL had created and sustained an artificial market where the prices were constantly going up. Chirag was one of the clients of the Noticee and was also instrumental in sustaining the market in Settlement Nos 6 and 8. However, the Noticee, when confronted with the charge of trading in such a manner, merely denied the said charge. However, a mere rebuttal without sufficient documentary evidence to substantiate the same is not tenable.
- 5.23 I also find that the trades executed by the aforementioned clients were circular in nature. The client Chirag was also part of such trades and had aided the other entities involved to sustain the market. In this regard, the Enquiry Officer has relied the dicta of the decision in Appeal No. 97 of 2002 Shri . Rajkumar Chainrai Basantani Vs. SEBI, the views of the SAT are reproduced below:

.....Analysing the trading pattern of the scrip, the Respondent had brought out the fact that top 5 brokers of BSE and NSE had formed a cartel and indulged in circular trading in the scrip so as to create artificial market in the scrip and also to maintain the price quote. Circular Trading is established if commonality of clients and their nexus with the

promoters is proved. In this case there was ample evidence including funds flow from the account of Shri Basantani to the account of the clients to suggest that circular trading in the scrip had taken place. The Respondent submitted that the Member is clearly guilty of indulging in circular trading by quoting examples. The persons/entities who have offered the shares in the auctions were the same clients who had traded in the scrip of SIL viz. Nagraj Kunder and Yogesh Panchal, Suhas Patil, and Shri Dinesh Patel etc (emphasis not supplied)

- 5.24 Upon a reading of the dicta of the Tribunal in the cases brought out above, it is clear that with the inter relationship between the entities in question being established, and a commonality of the clients and their nexus with the promoters of MFPL being established, there is reason enough to hold that the trading between these entities, acting in concert was primarily to create an illusion of trading with a view to boost volumes/price in the scrip of MFPL.
- 5.25 It would be relevant to note that the scrip quoting at Rs.15-16/- at the time of launch of the issue, rose to Rs 112.50 on August 30, 1996 from Rs 8.50 on June 6, 1996 i.e. just after a little more than 2 1/2 months. Realizing an undue rise in the price of the scrip, even the BSE had imposed margins and circuit filters in the said scrip. The last trade of Noticee was shares offered in auction in the month of August. That was the last trading month in the scrip of MFPL. Thereafter the trades in the scrip of MFPL were itself suspended by SEBI w.e.f. September 9, 1996.
- 5.26 The Enquiry Officer has also examined the contention of Noticee that they had executed trades for Chirag for a limited period and they had stopped trading for Chirag, after receiving the notice from the BSE, regarding an enquiry into the scrip of MFPL. I find that this stand is not tenable as Noticee had last traded for Chirag in settlement no. 8 i.e. from June 24, 1996 to July 5, 1996. This apart, there were a few other trades executed by Noticee for Khandwala Finstock in the scrip of MFPL and those offered in auction in settlement numbers 9 to 11. Later on the scrip was suspended for 3 days from September 2 to 4, 1996 and later suspended on September 9, 1996 till further notice. Considering the fact that scrip was listed only in the 6th settlement of the year 1996 i.e. on May 29, 1996 and suspended between September 2, 1996 and September 4, 1996 and finally on September 9, 1996, there was no question of Noticee executing trades after September 9, 1996. Hence the said contention of Noticee is not convincing.
- 5.27 As regards, their contention of trading only between the price of Rs.20-40/-, the Enquiry Officer stated that no proof of the same has been provided by Noticee even after they were specifically advised to submit the same. Even otherwise, the details of their trades executed for Khandwala Finstock clearly indicate that Noticee had traded till the 11th settlement, at which point of time the price of the scrip of MFPL was Rs.110/- approximately. Hence no reliance can be placed on the contention of Noticee of not having any role in the rise of the price of the scrip. I also observe that the Noticee was also benefited through its associated entity, Khandwala Finstock, by the false market created and sustained by the dubious dealings of entities including its client Chirag which were in the nature of circular trading and price rigging.
- 5.28 From the above background of trades, I have examined as to whether the Noticee was involved in the price and volume manipulation of the scrip of MFPL so as to create artificial market. In this regard, the Enquiry Officer had observed that the total paid up capital of MFPL consisted of 60,94,300 shares after the public issue. Out of these shares, the promoters of MFPL had cornered 48,26,300 shares constituting 80% of the post issue paid up capital. This meant that the floating stock was only to the extent of about 20%. It may be noted that the low volumes may absorb the liquidity of the scrip from the system and create artificial scarcity which would lead to the manipulation of the price and volume of the scrip.
- 5.29 It is pertinent to mention that at the relevant time BSE was taking many steps like levying special margins and consistently reversing circuit filter levels which ought to have sent a strong signal to the market that there is something suspicious in the trading in the scrip. Further, the scrip was just listed and this particular entity Chirag got registered with the Broker at about the same time the scrip came out for public issue. The entity was trading only in this particular scrip and the pattern of trading was also suspicious. These details are enough to raise concern for a prudent and responsible broker. The stock market system depends a lot on such prudence of the intermediaries. The brokers are the first line of monitoring and surveillance in the market. The failure at this level will weaken the fundamentals of the system and will harm its development to a safe market of international standards. In the instant case the Noticee did not exercise the due skill and diligence expected from them and failed to take any action even though there were enough indications suggesting clearly that the trading in the scrip by the client was suspicious. The low volume contribution as claimed by the Noticee in the instant case is not of much importance. In cases of circular trading, it is not always about large volumes, but about sustaining and creating an artificial market. In the instant case in settlement no. 6, the quantity sold by Rajesh Financial Services was 62500 shares, of which 15000 shares were bought by Chirag and the remaining shares were bought by Sneha Investments and Subhash Trading, all entities connected to promoters and introduced to the market participants by persons belonging to the Wallfort Group. When RFS is selling and if there is no entity like Chirag to buy such shares, the market RFS had created by such trades may not be sustaining even if Subhash Trading and Sneha Investments are still there, and the dynamics of the market would have been different in such case. Hence, the contention of small volume will not hold good. Also instead of taking action against the suspicious dealings of its client, the Noticee in fact tried to benefit out of the artificial market through its associated entity.
- 5.30 Further, I observe that the sellers were not able to deliver their shares of MFPL due to the low floating shares. As a result, their sale position got auctioned and the clients of the major brokers including the Noticee had offered the shares in the

auction and that too when the prices were actually rising. The following are the details of the shares delivered by the Noticee in auction:

St. No	Broker	Client	Net position	Delivery rec/ given out in payout	Adjusted against auction offer	Delivery received in auction	Qty. closed out	Other auction offer
7	Active	Chirag	16000	10400	3400	-	-	2200
8	Active	Chirag	14000	2800	7200	4000		

5.31 The Noticee contented that the quantum of their trades on behalf of their client was insignificant. Further, they stated that the trades attributed at settlement No.8 do not belong to them. I observe that the Noticee on behalf of Chirag has adjusted 3400 shares against the auction offer and received 10400 shares in auction and no delivery was received in auction. This aspect also indicates that trades were not genuinely carried out by them.

5.32 Further, the Enquiry Officer has also pointed out the date of opening of account of Chirag with Noticee which was introduced by Shri Ashok Bharadia of WSFL. As pointed out by Shri Vimal Khandwala, Director of Noticee vide his statement made on June 27, 2002, the trading account of Chirag was operational from June 19, 1996 to August 21, 1996. This period is to be compared with the settlement wise / date wise trading details. Noticee commenced trading for Chirag from settlement no. 6 of 1996 which is effective from May 26, 1996 to June 7, 1996. The date of opening of trading account with Noticee cannot be a date later to the date when the trades were effectively executed by Noticee. However, with the same being a reality and as admitted by the Director of Noticee, the veracity of the trades executed by Noticee, prior to the opening of the trading account of Chirag on June 19, 1996 with Noticee needs to be viewed seriously. This also raises the moot point as to whether the trades executed for and on behalf of Chirag were through a fictitious trading account. The fact that the said trading account was closed on August 21, 1996 is indicative that there was a specific purpose of having opened the trading account in the first place. The events above indicate that the purpose was of executing trades only in the scrip of MFPL. The Noticee in its reply to the post enquiry show cause notice submitted that when the statement was recorded, they inadvertently stated that the date of opening of trading account of Chirag was on June 19, 1996 which is only the bill date whereas the date of opening the trading account of Chirag was on June 7, 1996. For establishing the said contention, they have only produced a copy of the bill dated June 19, 1996 which is not sufficient to prove the said contention. Noticee ought to have produced their register to show that the trading account was opened only on June 07, 1996. Further, it is pertinent to mention that the said June 07, 1996 was the last date of settlement No.6 of 1996. Hence, the Enquiry Officer rightly held that the transactions of Noticee along with other persons acting in concert with them as a whole, in the manner discussed above, gave a misleading appearance of trading in the scrip of MFPL, resulting in the creation of an artificial market and volumes and thus enhanced liquidity. Noticee is thus guilty of having indulged in facilitating the creation of artificial trade volumes and raising the price of the scrip of MFPL and has violated the provisions of the PFUTP Regulations. The same was effected in the following manner:

- a) Opening of the trading account of Chirag much later to the date of execution of the trade
- b) Trading extensively in the same scrip on behalf of a client i.e. Chirag for settlements 6-8 and an associate entity i.e. Khandwala Finstock for settlements 9-11 i.e. entirely during the period of launching of the public issue from May 29, 1996 almost till the scrip was finally suspended for trading in September 9, 1996.
- c) The above was facilitated due to the nexus between the broker/client/promoters of MFPL.
- d). Trades executed in the circular manner between the same set of clients and brokers.
- e) Offering of shares in auction at manipulated prices.

5.33 Further, in the process of perpetuating these artificial trades, Noticee has also failed to exercise proper skill, care and diligence, required of a broker as already discussed earlier. The Noticee further failed to verify the bonafides and financial worthiness of the client, Chirag. As a registered broker of BSE, Noticee was fully aware of the Rules and Regulations of SEBI. In this regard, it is pertinent to note that Circular No SMD-1/23341 dated November 18, 1993 was in force even prior to the relevant time and which specifically provided a set of precautions to be exercised by member brokers while dealing on behalf of clients. These precautions emphasize upon the need for proper introductory procedure and care, while dealing with their clients with a view to protect the interest of the member brokers, encourage transparency and discipline in their working etc. In view of this Circular and the clauses of Code of Conduct for the Stock Brokers, it was the bounden duty of Noticee to verify the antecedents of its clients and their financial worthiness. I find that Noticee had failed to observe the clauses of Code of Conduct by not maintaining the standards of integrity, promptitude and fairness required of a broker.

5.34 In the light of above findings, it is clearly established that the Noticee failed to exercise due care, skill and diligence in the conduct of their professional responsibility and the same is in violation of clause A(2) of Schedule II read with Regulation 7 of Stock Brokers Regulations which reads as under:

A(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.

5.35 Further, it is established that the Noticee transacted in the scrip of MFPL with an intention to create artificial price and volumes and misutilised the stock exchange mechanism. Noticee is responsible for creating false market and misleading appearance of trading in the market, executed transactions which are not genuine trade transactions and was done with the

intention to inflate or cause fluctuations in the market price of the scrip. Thus Noticee violated Regulation 4(a), (b) and (c) of PFUTP Regulations which reads as follows:

Prohibition against Market Manipulation

4. No person shall -

(a) effect, take part in, or enter into, either directly or indirectly, transactions in securities, with the intention of artificially raising or depressing the prices of securities and thereby inducing the sale or purchase of securities by any person;

(b) indulge in any act, which is calculated to create a false or misleading appearance of trading on the securities market;

(c) indulge in any act which results in reflection of prices of securities based on transactions that are not genuine trade transactions;

- 5.36 Under section 11 of the SEBI Act, SEBI can take steps to protect the interests of investors and to regulate the securities market inter alia by registering and regulating the working of stock brokers. If the regulatory requirements are violated by the stock brokers without attracting any action, the measures initiated by SEBI for regulation of the stock brokers would be rendered nugatory and the regulatory function would be jeopardized. It is to be noted that indulgence of the Noticee in the transactions which are prohibited can not be allowed as these transactions will have a detrimental effect on the functioning and integrity of the securities market. Having considered all aspects of the matter, I find that the penalty of suspension of certificate of registration of the Noticee for a period of one months recommended by the Enquiry Officer is reasonable.

6.0 ORDER

- 6.1 In view of above facts and circumstances of the matter and in exercise of the powers conferred upon me under Section 19 of the Securities and Exchange Board of India Act, 1992 read with Regulation 13(4) of SEBI Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002, I hereby impose a minor penalty of suspension of certificate of registration issued to the Noticee M/s Active Finstock Pvt. Ltd, a registered broker of the Bombay Stock Exchange Ltd. with SEBI registration no. INB 010849331 for a period of one month.
- 6.2 This order shall come into force immediately on the expiry of twenty one days from the date of this order.

Place: Mumbai
Date: May 24, 2007

V. K. CHOPRA
WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA