

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER UNDER REGULATION 13 (4) OF SECURITIES AND EXCHANGE BOARD OF INDIA (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002 AGAINST M/S. JYOTISH BHOGILAL STOCK BROKERS PRIVATE LIMITED, BEARING SEBI REGISTRATION NUMBER INS 010736432/01-05028, REGISTERED AS SUB-BROKER TO M/s. PRABHUDAS LILADHAR PRIVATE LIMITED, MEMBER, THE STOCK EXCHANGE, MUMBAI AND THE NATIONAL STOCK EXCHANGE, IN THE MATTER OF M/s. CONTINENTAL CONTROLS LIMITED

WTM/TCN/ ID6/27/06/2007

1.0 BACKGROUND

- 1.1 The Securities and Exchange Board of India (SEBI) conducted an investigation into the abnormal price and volume rise in the scrip of M/s. Continental Controls Ltd. (hereinafter referred to as "the company" or "CCL") during July 2002. It was alleged that the increase in price and volumes in the said scrip was a result of manipulation in the scrip by various market players. During the course of the investigations it was observed that M/s. Jyotish Bhogilal Stock Brokers Private Limited, registered as a sub-broker to M/s. Prabhudas Liladhar Private Limited, Member, The Stock Exchange, Mumbai (herein after referred to as 'BSE') and the National Stock Exchange (NSE) was also involved in dealing in the said scrip. CCL published an advertisement in 'The Business Standard' and other newspapers stating that on 27th July 2002 the company's board meeting was to be held to consider the buy back of 12, 00, 000 shares (15% of the paid up equity capital) at Rs. 25 per share. It is worth noting that the price of the scrip during 1st week of July 2002 was only around Rs. 5 – Rs. 6 and book value of the scrip was around Rs. 11.50. The scrip witnessed trading of a volume of more than 8 lakh shares on 10th July 2002 with price touching Rs. 12.75. Further on 11th July 2002, the day on which the said advertisement was published in Economic Times and Mumbai Samachar, trading in the scrip of the company was at a record volume of around 10 lakh shares at BSE. It was suspected that the rise in the price of the scrip of the company was not natural but manipulated by certain individuals who had acquired shares of the company in off market deals at the price of around Rs. 2 – Rs. 2. 50 in April / May 2002; they were manipulating the price of the scrip to sell their shareholding in the market. Investigations revealed that the company did not have adequate resources to buy back shares of the company as required under the provisions of Section 77-A of the Companies Act, 1956. It was further observed that the Board of the company at its meeting held on 27th July 2002 had deferred the proposal of buy back of shares, but this information was not made public.
- 1.2 Investigations conducted by SEBI found that during the period 1st June 2002 and 31st July 2002, M/s. Jyotish Bhogilal Stock Brokers Pvt. Ltd. (hereinafter referred to as "the sub-broker"), bearing SEBI registration No. INB 020916831 and registered as sub-broker with M/s. Prabhudas Liladhar Private Limited (hereinafter referred to as "PLPL") a member of BSE and NSE, had bought 1, 41, 100 shares and sold 2, 00, 028 shares on BSE. Trading of the sub-broker in this scrip contributed around 99% of the total quantity traded by PLPL. Further as the sub-broker had not executed client registration forms properly, signature of client was not available. While the sub-broker started trading on behalf of one Shri Mahesh M. Shah from 8th July 2002, the member client agreement was signed only on 17th July 2002 by which time the sub-broker had made a payment of Rs. 25 lakh and as admitted by the sub-broker, had received delivery of shares around 1 lakh from Shri Mahesh M. Shah.
- 1.3 It was further found that Shri Mahesh M. Shah had purchased 40, 000 shares which were transferred into the account of one Shri Atul B. Shah, Proprietor of M/s. Charmi Investments. It was further found that the shares sold by Shri Mahesh M. Shah were delivered from three accounts namely Shri Mukesh Bachubhai Shah, Shri Ashish P. Shah and Shri Vinod N. Desai to the account of the sub-broker. Details of such transfers are as under

DELIVERIES FROM / TO (DP ID / CLIENT A/C NO.)	DATE	NO. OF SHARES
Mukesh Bachubhai Vadecha (Pravin Ratilal / 10172288)	11-07-02	-84,277
Ashish P. Shah (Khandwala / 10003169)	13-07-02	-1,500
Vinod N. Desai (Khandwala / 10039063)	15-07-02	-11,651
Total		97, 428

- 1.4 It was found that the sub-broker made payment of around Rs. 30 lakh through cheques on various dates for shares sold by Shri Mahesh M Shah. This amount was not credited in the account mentioned in client introduction form of Shri Mahesh M. Shah, but to a different account with same bank.
- 1.5 It was alleged that the sub-broker did not exercise due skill, care and diligence in its dealings with its clients thereby contravening the Code of Conduct prescribed for sub-brokers as given under Schedule II read with regulation 15 of Securities and Exchange Board of India (Stockbrokers and sub-brokers) Regulations, 1992 (hereinafter referred to as "Brokers Regulations").

2.0 ENQUIRY PROCEEDINGS

- 2.1 In view of the alleged irregularities committed by the sub-broker, Chairman, SEBI, vide his order dated 1st October 2004 appointed an Enquiry Officer to enquire into its affairs. The Enquiry Officer was to enquire into the alleged contraventions of the various provisions of SEBI Act, 1992, SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995 and SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992 committed by the sub-broker and to submit a report to the Board based on his enquiry. A show cause notice dated 06-04-2005 was issued to the sub-broker in terms of Regulation 6(1) of the SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002, wherein the allegations against it were set out. The sub-broker was also heard by the Enquiry Officer in accordance with Regulation 9 of the Enquiry Regulations, wherein Shri Aditya Bhansali represented the sub-broker and made the submissions. Enquiry Officer after conducting requisite enquiry submitted a report dated 30th July 2005 to SEBI recommending a minor penalty of censure be imposed on the sub-broker for contravention of the provisions of Clause A(1) and (2) of the Code of Conduct for sub-brokers prescribed in Schedule II read with Regulation 15 of SEBI (Stock Brokers and Sub-brokers) Regulations, 1992.

3.0 SHOW CAUSE NOTICE AND REPLY

- 3.1 On submission of said Enquiry Report, as required by regulation 13 (2) of Securities and Exchange Board of India (Procedure for holding Enquiry by Enquiry Officer and imposing penalty) Regulations, 2002, a show cause notice dated 24th August 2005 was issued to the sub-broker. The sub-broker vide letters dated 10th September 2005 and 3rd October 2005 replied to the said show cause notice inter alia submitting as follows
- a). Delay in signing of the member client agreement was an inadvertent mistake and was merely a technical lapse. Moreover there was only an inadvertent delay in signing the client registration agreement besides which all the necessary details were available.
 - b). Adequate due diligence as expected from a prudent broker has been exercised. There was no wanton attempt to circumvent any rules or regulation and there is unfair advantage derived or any loss or damage caused to anyone.
 - c). Even minor penalty of Censure is not warranted in the facts and circumstances of the instant case.

4.0 CONSIDERATION OF ISSUES

- 4.1 I have carefully considered the Enquiry Report, show cause notice issued to the sub-broker and submissions made by the sub-broker in response to the show cause notice. Since the Enquiry Officer has recommended only a minor penalty of censure, I proceed to consider the issues on merit as a hearing to the sub-broker is not necessary.
- 4.2 I note that the sub-broker had in its reply submitted that the delay in obtaining signature of client on member client agreement is mere technical delay. The pre-condition to trade on behalf of a client is to enter into a valid agreement with client and needless to say in the instant case an agreement without signature of one part is not valid. Given the situation the conduct of the sub-broker, trading on behalf of a client even before entering into a valid agreement does not remain a mere technicality.
- 4.3 I note that delivery obligations of one client had been met by entities other than the client who had traded in the scrip of the company. As mentioned above, delivery obligation of Shri Mahesh M Shah was met by shares received from the accounts of Shri Mukesh Bachubhai Vadecha, Shri Ashish P. Shah and Shri Vinod N. Desai. I find that the conduct of the sub-broker in knowingly accepting shares of third parties in respect of the delivery obligation of its client indicates that the sub-broker failed to maintain integrity. I note that the sub-broker has failed to exercise due diligence which is observed from the hands-off attitude of the sub-broker in not bothering to obtain the signature of their client and adjusting trades of client with trades of another and stating that was done on request of clients. I find that such lapses would pose a threat to the safety of the securities market. Since in this case enquiry officer did not find the sub-broker related to the client or being involved in any irregular activity, he has recommended a minor penalty to be imposed on the sub-broker and I agree with the finding and recommendation of enquiry officer that the sub-broker did not exercise due skill and diligence while executing client registration agreement and a minor penalty of censure should be imposed. Thus, I find that the sub-broker is liable for violation of Clause A (2) of the Code of Conduct prescribed for sub-brokers under Securities and Exchange Board of India (Stockbrokers and sub-brokers) Regulations, 1992.
- 4.4 I note that the sub-broker has submitted that the rules of natural justice has not been followed in their case, since the investigation report and the depositions of various persons have not been furnished to them. In my view, since the extracts of the investigation report are already provided to the sub-broker vide the show cause notice dated 06-04-2005 and there are no adverse findings against the sub-broker based on the depositions of various persons, there is no violation of the principles of natural justice. I also note that the sub-broker has admitted that they have by mistake not obtained the signature of a client in the member-client registration form and that the signature was obtained later. Thus the above instances would prove that the sub-broker has not properly exercised due care and diligence as they ought to have. This

lapse of the sub-broker is definitely against the provisions of Clause A 2 of the code of conduct prescribed for a sub-brokers under the SEBI (Stockbrokers and Sub-brokers) Regulations, 1992.

- 4.5 The sub-broker vide his submissions has relied on an observation made by the Hon'ble Supreme Court in Hindustan Steel Vs. State of Orissa (AIR 1970 SC 253), that in a quasi-judicial criminal proceeding, penalty will not be ordinarily imposed unless the party had acted deliberately in defiance of law. The proceeding in question is no doubt a quasi judicial proceeding but civil in nature and the 'mens rea' or the mental element has no relevance in such cases. The same view has been enunciated recently by the Hon'ble Supreme Court in a landmark case. The Hon'ble Supreme Court, while dealing with the penalty levied under Chapter VIA of SEBI Act, in SEBI vs. Shriram Mutual Fund (2006) 68 SCL 216(SC) held that "penalty is attracted as soon as the contravention of the statutory obligation is established and hence, the intention of the parties committing such violation becomes wholly irrelevant since the penalties are imposed for breach of the civil obligations under SEBI Act". The Hon'ble court further held that the ratio laid down in Hindustan Steels Ltd. vs. State of Orissa AIR 1970 SC 253 is not applicable to the imposition of civil liabilities under SEBI Act and the Regulations made there under. Thus, the reliance on the ratio of Hindustan Steel Case supra by the sub-broker is not applicable to the present case before me. The sub-broker, further, had also cited cases to substantiate its stand that the quantum of penalty needs to be in accordance with the gravity of the violations committed. I find that the Enquiry Officer was reasonable in recommending a penalty of "Censure" for the technical and procedural lapses as admitted by the sub-broker. Thus I have no reason to differ with the findings or the quantum of penalty recommended by the Enquiry Officer.

5.0 ORDER

- 5.1 Therefore, in view of the above discussion, I, in exercise of powers conferred upon me in terms of Section 19 of the Securities and Exchange Board of India Act, 1992 read with regulation 13 (4) of Securities and Exchange Board of India (Procedure for holding Enquiry by Enquiry Officer and imposing penalty) Regulations, 2002, hereby impose a minor penalty of censure on M/s. Jyotish Bhogilal Stock Brokers Pvt Ltd, Sub-broker bearing SEBI registration No. INS 010736432/01-05028 registered as a sub-broker to M/s. Prabhudas Liladhar Pvt. Ltd., Member, The Stock Exchange, Mumbai and The National Stock Exchange.

Date: 15.06.2007

Place: Mumbai

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