

SECURITIES AND EXCHANGE BOARD OF INDIA

Coram: Dr. T. C. Nair, Whole Time Member

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. Park Light Investments Private Limited, bearing SEBI broker registration No. INB011037836, Member, The Stock Exchange, Mumbai, in the matter of M/s. Continental Controls Ltd.

WTM/TCN//ID6/ 11/06 /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. Park Light Investments Private Limited (herein after referred to as 'broker' or 'PLIP'), a member of The Stock Exchange, Mumbai (herein after referred to as "BSE") was also involved in dealing in the said scrip. CCL had published an advertisement in 'The Business Standard' and other newspapers stating that on 27th July 2002 that a 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 volume of more than 8 lakhs 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 a record volume of around 10 lakhs 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 and were manipulating the price of the scrip to sell their shareholding in the market. It was also observed 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 Indian Companies Act. It was further observed that the Board of the company in its meeting held on 27th July 2002 had deferred the proposal for buy back of shares. However this information was not made public.
- 1.2 Investigation conducted by SEBI found that, during the period 1st June 2002 and 31st July 2002, the broker had bought 2, 57, 641 shares and sold 2, 31, 175 shares of the company with a net delivery of 26, 466 shares. The broker had not executed client registration forms properly. In case of Shri Mahendra Amruthlal Shah, he had not signed, his photograph was not affixed on the client registration form, his proof of identity was not obtained and the signature of the introducer of Shri Mahendra Shah was not available. In addition to this, on 5th June 2002 itself the broker had purchased 12, 900 shares on behalf of Shri Mahendra Shah and the client agreement was signed by Shri Mahendra Shah only on 10th July 2002. In case of Raju B Vadecha, his signature was missing on the client registration form.
- 1.3 Further, Shri Mahendra A. Shah purchased 10, 650 shares on 4th June 2002, however, the trade log of the broker reflected as if these share were purchased by another client Shri Raju B. Vadecha. It was further found that net quantity of shares purchased by Shri Raju B. Vadecha and Shri Mahendra Shah were not credited into respective client accounts but were transferred to the account of yet another client of the broker, Shri Sanjiv P. Shah (M/s. H Nyalchand Financial Services Ltd., A/c no. 10006265). In view of the above, it was alleged that the act of transferring shares to an account other than respective client account was in violation of SEBI Circular SMDRP/Policy/Cir-05/2001 dated 1st February 2001.
- 1.5 It was also alleged that the broker did not exercise due skill, care and diligence in its dealings with its clients which was in violation of clause A (1) and (2) Code of Conduct as given under Schedule II read with regulation 7 of Securities and

2.0 ENQUIRY PROCEEDINGS

- 2.1 In view of the alleged irregularities committed by the broker, Chairman, SEBI, vide his order dated 1st October 2004 appointed an Enquiry Officer to enquire into the affairs of the broker. 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 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 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 them were set out. The broker was also heard by the Enquiry Officer in accordance with Regulation 9 of the Enquiry Regulations, wherein Shri Uday Vora and Shri Aditya Bhansali represented the broker and made their submissions. The Enquiry Officer after conducting the enquiry then submitted his report dated 28th July 2005 to the Board and recommended a minor penalty of 'censure' be imposed on the broker for its contravention of Clause A(2) of the Code of Conduct for Stock Brokers prescribed in Schedule II read with Regulation 7 of SEBI (Stock Broker and Sub-Broker) Regulations, 1992.

3.0 SHOW CAUSE NOTICE AND REPLY

- 3.1 On submission of the Enquiry Report, a show cause notice dated 24-08-2005 was issued to the broker in accordance with Regulation 13 (2) of Securities and Exchange Board of India (Procedure for holding Enquiry by Enquiry Officer and imposing penalty) Regulations, 2002. The broker replied vide its letters dated 19th September 2005 and 24th September 2005 to the said show cause notice and submitted the following among others,

- 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 no 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.

- 3.2 I am of the view that the hearing of the broker before me is not necessary in the instant case as the Enquiry Officer has recommended only a minor penalty of 'Censure' against the broker and I proceed to consider the issues on merit.

4.0 CONSIDERATION OF ISSUES AND FINDINGS

- 4.1 I have carefully perused the show cause notice, the Enquiry Report and the submissions made by the broker through their replies.

- 4.2 I note that the broker in its reply submitted that delay in obtaining signature of client on member client agreement is a technical delay. However from the record it is seen that it was not just signature but photograph of client was also not available on record. The pre-condition to trade on behalf of a client is to enter into a valid agreement with client and

needles to say in the instant case an agreement without photograph and signature of one part is not valid. Given the situation the conduct of the broker trading on behalf of a client even before entering into a valid agreement does not remain a mere technicality.

- 4.3 I further note that the broker had admittedly adjusted shares of one client with shares of another client. I note that shares purchased by Shri Raju B. Vadecha and Shri Mahendra Shah were credited into the account of one Shri Sanjiv P. Shah of M/s. H. Nyalchand Financial Services. Ltd., bearing A/c No. 10006265. It is the duty of broker to credit shares purchased by a client into the account of same client. In the instant case however, the broker has credited shares of one client to another account and justified it saying it was done on the instruction of the client. The Enquiry Officer has accepted the contention of the broker and I do not wish to differ on this count.
- 4.4 I note that the functioning of the broker brings to focus the question of exercise of due diligence by the broker and more so the intention of the broker to comply with Broker Regulations in respect of due diligence. This is observed from the hands-off attitude of the broker not bothering to collect photograph, proof of identity or signature of clients and adjusting trades of client with trades of other clients and stating that it was done on request. I note that, such lapses would pose a threat to the safety of securities market. However since in this case Enquiry Officer did not find the broker related to the client or being involved in any irregular activity has recommended a minor penalty to be imposed on the broker.
- 4.5 I find that there is no enough material on record to conclude that the broker had nexus with clients namely, Shri Sanjiv P Shah, Shri Raju B. Vadecha and Shri Mahendra A. Shah except the broker client relationship and that the broker was part of any conspiracy with the clients and indulged in any market manipulation along with the clients.
- 4.6 I note that the broker has submitted that the rules of natural justice has not been followed in its 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 broker vide the show cause notice dated 06-04-2005 and there are no adverse findings against the broker based on the depositions of various persons, there is no violation of principles of natural justice. I also find that the broker has admitted that it had by mistake not obtained the signatures of clients Shri Raju B Vadecha and Shri Mahendra Shah in the member-client registration form and that the signatures were obtained later. Thus the above instances would prove that the broker had not properly exercised due care and diligence as they ought to have. This lapse of the broker is definitely against the code of conduct prescribed for a stock broker. I agree with the findings and recommendation of Enquiry Officer that the broker did not exercise due skill and diligence while executing client registration agreement and that a minor penalty of censure should be imposed. I have no hesitation in holding the broker liable for violating the provisions of Clause A (2) of the Code of Conduct prescribed for stock brokers under Regulation 7 of the Securities and Exchange Board of India (Stockbrokers and sub-brokers) Regulations, 1992.
- 4.7 The broker has cited the case of Hindustan Steel V. State of Orissa (AIR 1970 SC 253), wherein the broker has relied on an observation made by the Hon'ble Supreme Court that "in a quasi-judicial criminal proceeding, penalty will not be ordinarily imposed unless the party had acted deliberately in defiance of law". I find that 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 by the Hon'ble Supreme Court, recently 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 Supreme Court further held that the ratio laid down in Hindustan Steels Ltd. supra 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 ibid by the broker is not applicable to the present case before me. The broker, further, had 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 broker. Thus I have no reason to differ with the findings or the quantum of penalty recommended by the Enquiry Officer. In view of the above, the broker is liable for violating the provisions of Clause A (2) of the Code of Conduct prescribed for stock brokers under Regulation 7 of the Securities and Exchange Board of India (Stockbrokers and sub-brokers) Regulations, 1992.

5.0 ORDER

- 5.1 Therefore, 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. Park Light Investment Private Limited, bearing SEBI broker registration No. INB011037836, Member, The Stock Exchange, Mumbai.

Date: 13.06.2007

Place: Mumbai

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