

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA
CORAM: PRASHANT SARAN, WHOLE TIME MEMBER

ORDER

Under regulation 28 read with regulation 35 of the Securities and Exchange Board of India (Intermediaries) Regulations, 2008

In the matter of irregularities in the Initial Public Offerings

In respect of Karvy Stock Broking Limited, a stock broker registered with SEBI with Registration Nos. INB 230770138, INB 010770130 and INB260770137

Date of hearing: April 07, 2015

Appearance:

For Karvy Stock Broking Limited:

1. Mr. Vinay Chauhan, Advocate
2. Mr. C. Parthasarathy, Chairman and Managing Director, Karvy Stock Broking Limited
3. Mr. Muthuswamy Iyer, Head (Compliance), Karvy Stock Broking Limited
4. Mr. CL. Viswanath, Head-Legal, Karvy Stock Broking Limited
5. Mr. V. Mahesh, Karvy Stock Broking Limited
6. Mr. K. C. Jacob, Advocate
7. Mr. Apurv Gupta, Advocate

For the Securities and Exchange Board of India: Mr. T. Vinay Rajneesh, Assistant General Manager, Mr. Ankit Bhansali, Assistant General Manager and Mr. Abhiraj Arora, Manager

1. This proceeding is in respect of **Karvy Stock Broking Limited** (stock broker) [hereinafter referred to as "the **noticee**" or "**KSBL**"] pursuant to and in compliance with the Order dated January 21, 2015 passed by the Hon'ble Securities Appellate Tribunal ("Hon'ble SAT") in Appeal no. 66 of 2014 – KSBL vs. Securities and Exchange Board of India ("SEBI").

2. A brief background of the matter is as follows:

- (a) SEBI had conducted an investigation into the alleged irregularities in the transactions in the shares that were issued in the Initial Public Offerings ("IPOs") by 21 companies during the period 2003-2005. During the investigation, it was observed that many individuals/entities (hereinafter referred to as "the key operators") had opened various demat accounts (hereinafter

referred to as "afferent accounts") in fictitious/benami names and made large number of applications in the IPOs in the category of retail investors (*each of the applications being of small value as to make it eligible for allotment under the retail category*). These key operators were found to have cornered/acquired the shares issued in the IPOs by using these fictitious accounts. On allotment of shares under the retail category, the same were transferred to the demat accounts of the key operators who subsequently transferred the shares in off-market to ultimate beneficiaries who were the financiers in the IPOs.

- (b) The investigations *prima facie* observed that the "Karvy Group" comprising of - Karvy Stock Broking Limited ("KSBL"), Karvy Consultants Limited ("KCL"), Karvy Computershare Private Limited ("KCPL"), Karvy Securities Limited ("KSL") and Karvy Investor Services Limited ("KISL"), had allegedly assisted, aided and abetted the key operators in cornering the shares issued in the IPOs.
- (c) Pending investigation, SEBI had passed *ex-parte interim orders* dated December 15, 2005, January 12, 2006 and April 27, 2006, wherein directions were issued against various persons, entities and intermediaries including entities of the Karvy Group. The said Orders also served as show cause notices to those entities. Pursuant to the passing of the Order dated April 27, 2006, SEBI had afforded an opportunity of personal hearing *inter alia* to KSBL and thereafter passed the Order dated May 26, 2006, directing KSBL (*in its capacity as a stock broker*) not to undertake any proprietary trades in securities, either off-market or on market, pending enquiry and passing of final orders.
- (d) SEBI had initiated enquiry proceedings under the SEBI (Procedure for Holding Enquiry and Imposing Penalty) Regulations, 2002 ("the Enquiry Regulations") against the noticee. A show cause notice dated September 22, 2006 ("the pre-enquiry SCN") was issued by the Enquiry Officer. The pre-enquiry SCN was a common notice issued to Karvy Stock Broking Limited (Depository Participant) [referred to as KSBL-DP], the noticee [KSBL-stock broker] and Karvy Computershare Private Limited (Registrar and Share Transfer Agent –referred to as 'KCPL'). Thereafter, on completion of the enquiry, the Enquiry Officer found that the noticee had contravened the provisions of regulations 3 and 4(1) of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 (hereinafter referred to as "the PFUTP Regulations"), Clause A (1), (3) and (4) of the Code of Conduct

prescribed for stock brokers under schedule II of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992 (hereinafter referred to as “the Stock Broker Regulations”) read with regulation 7 thereof and the provisions of the SEBI (Disclosure and Investor Protection) Guidelines, 2000 (hereinafter referred to as "the DIP Guidelines"). In view of his findings, vide Report dated March 15, 2007, the Enquiry Officer recommended that the certificate of registration granted to KSBL (*in its capacity as a stock broker*) be suspended for a period of three months.

- (e) Thereafter, SEBI issued a show cause notice dated May 04, 2007 (“the SCN”), which enclosed a copy of the Enquiry Report, advising the noticee to show cause as to why appropriate penalty including the penalty as recommended by the Enquiry Officer should not be imposed on it. The noticee submitted its reply dated May 19, 2007 and written submissions dated June 06, 2007.
- (f) Meanwhile, Enquiry Reports were also submitted in the proceedings initiated against KSBL-DP and KCPL. After considering all the three Enquiry Reports, SEBI disposed of the proceedings vide a common Final Order dated June 22, 2007, wherein the following directions were issued:
 - (i) The certificate of registration of the noticee [i.e., KSBL-*stock broker*] was suspended for a period of three months. The said direction was to come into force immediately on expiry of 21 days from the date of the Order.
 - (ii) KSBL-DP was prohibited from opening fresh demat accounts till December 31, 2007, with immediate effect.
 - (iii) KCPL was prohibited from acting as a registrar to an issue for a period of nine months. As KCPL had already undergone the prohibition vide directions issued vide the SEBI Order dated April 27, 2006, there were no further directions against KCPL.
- (g) KSBL filed two appeals (*one in its capacity as a DP and other as a stock broker*) - nos. 75 and 111 of 2007 and KCPL filed an appeal (no. 153 of 2007) against the aforesaid common Order dated June 22, 2007 before the Hon'ble SAT. The appeals were disposed of by the Hon'ble SAT vide Order dated June 30, 2008, whereby the matters were remanded to SEBI with a direction to pass three separate orders on the three show cause notices issued. The following were also observed/directed by the Hon'ble SAT:

"..... It is, however, made clear that while passing the fresh orders the wholetime member shall take into account only the material that is already on the record and will not permit either party to produce any fresh material or file fresh replies or written submissions. He will, however, grant a fresh oral hearing to the parties and take into consideration the replies and written submissions already filed. The parties will however be at liberty to cite case law in support of their respective submissions. The wholetime member while passing the fresh orders shall not be influenced by any observation or finding recorded in the impugned order. We also make it clear that we have not decided any issue on merits and, therefore, all the issues raised by the parties remain open to be decided afresh by the learned wholetime member in accordance with law. In case the final order(s) were to go against the appellant(s), the same shall not be given effect to for a period of four weeks from the date of receipt thereof by the appellant(s)."

[Emphasis supplied]

(h) Pursuant to the above order of the Hon'ble SAT, the noticee (KSBL-stock broker) filed an application to settle the instant enforcement proceeding by way of a consent order. However, the application was rejected and the same was accordingly informed to the noticee. Thereafter, the proceeding initiated against the noticee was resumed and opportunities of personal hearing were afforded to it. The proceedings then culminated in the SEBI Order dated March 14, 2014 ("the **SEBI Order**"), which prohibited the noticee, for the reasons stated therein, from taking up any new assignment or contract or launch a new scheme (i.e., not to take new clients/customers) for a period of 6 months in respect of its business as a stock broker. This Order of SEBI was challenged by the noticee before the Hon'ble SAT, which was disposed of vide Order dated January 21, 2015, *inter alia* with the following observations/directions:

"9. Accordingly, the impugned order of SEBI dated 14/3/2014 is quashed and set aside and the matter is restored to the file of SEBI for passing fresh order on merits after giving an opportunity to the Appellant to cross-examine Mr. Devi Dutt, if SEBI chooses to rely upon the said statement of Mr. Devi Dutt.

10. In view of the fact that considerable time has elapsed from the date of the alleged violation, we direct SEBI to pass appropriate order on merits as expeditiously as possible and preferably within a period of four months from today. All contentions kept open.

11. Appeal is disposed of in the above terms with no order as to costs".

(i) SEBI, in compliance with the Order of Hon'ble SAT, considered the statement of Mr. Devi Dutt and informed the noticee, vide letter dated March 13, 2015, that SEBI shall not refer or rely on the statement of Mr. Devi Dutt in the present proceedings. The noticee was afforded an opportunity of personal hearing on March 27, 2015, which was rescheduled to April 07, 2015 as per the noticee's request.

(j) In the personal hearing held on April 07, 2015, the noticee appeared before me through its authorized representatives. Mr. Vinay Chauhan, Advocate and the noticee's Chairman and Managing Director, Mr. C. Parthasarathy made oral submissions, which were reiterated vide Written Submissions dated April 20, 2015. It was stated that these submissions are in addition to and in continuation of the noticee's earlier submissions made in the proceedings.

3. As directed by the Hon'ble SAT, I proceed to consider the case with respect to the noticee for passing a fresh order on merits without referring or relying upon the statement of Mr. Devi Dutt. I have considered the SCN dated September 22, 2006, the Enquiry Report dated March 15, 2007, post-enquiry SCN dated May 04, 2007 and the submissions made by the noticee. The submissions made by the noticee are dealt with while dealing with the related charge/issue against the noticee.

4. Before proceeding with the charges, the following needs to be highlighted. In the IPOs launched during 2003-2005, there was widespread cornering of retail quota of shares of the respective companies by certain key operators. The cornering were done with the aid of thousands of afferent accounts (fictitious/benami demat accounts opened solely to apply under retail quota in IPOs). After applying for shares under retail category through multiple fictitious/benami names and on allotment of shares in the afferent accounts, the shares were then transferred to the ultimate beneficiaries who offloaded the same on the listing day and made huge profits. SEBI had initiated disgorgement proceedings against those persons who were found to have made unlawful monetary gains through this modus operandi of cornering of retail category shares and offloading the same.

During the entire process, it is seen that several afferent accounts were *inter alia* opened with KSBL-DP. KCPL acted as the Registrar to an Issue in few of the IPOs.

The role of Karvy entities in the IPOs and in transactions thereafter was summarized in the following words in the Order dated February 03, 2014 passed against KCPL in the matter:

“Admittedly, the Karvy group entities were associated in various IPOs, in different roles that are required to be performed in relation to an IPO application. Starting with the role of DP who opened demat accounts, DP/ stock broker who introduced the bank accounts, the financier belonging to Karvy group who arranged finance to the key operators namely Ms. Roopalben Panchal, Purushottam Budhwani, Manoj Seksaria etc., the stock broker/ syndicate member who

undertook the bidding in IPOs, the RTI who prepared refunds, the DP who transferred the shares on allotment of the same to the demat account of the same set of key operators and ending with the sale of shares through its stock broking arm, one is able to identify the presence of Karvy group entities in the entire scheme of activities of the IPOs.”

Further, the SEBI Order dated January 28, 2014 passed against KSBL-DP and Order dated February 03, 2014 passed against KCPL have attained finality, as appeals have not been preferred in respect of the above SEBI Orders.

5. As per the SCN issued by the Enquiry Officer and the Enquiry report, the following are the allegations against the noticee:

- a) introduction of Bank accounts
- b) the noticee who is a stock broker and depository participant had blatantly opened large number of demat accounts
- c) sale of shares of key operators in the securities market
- d) nexus with other Karvy group entities and had aided and abetted the key operators in cornering shares and selling them in the market.

6. The SCN dated September 22, 2006 issued to the noticee *inter alia* alleged that the noticee had introduced large number of savings bank accounts to the bank for the purpose of arranging IPO finance from banks which facilitated the key operators to make multiple IPO applications for cornering shares in various IPOs. In this regard, the SCN alleged-

(a) *“68. Investigations also revealed that Karvy Stock Broking Ltd (KSBL) had introduced large savings bank accounts to BhoB Worli / Goregaon / Ahmedabad branches for this purpose of arranging IPO finance from banks, which facilitated the Key Operators (including D B Mehta) to make multiple applications in the IPOs for concerning the shares in various IPOs. Besides it is alleged that KSBL which is also a stock broker-depository participant had blatantly opened large number of afferent demat account (benami fictitious) in connivance with key operators in utter disregard/ defiance of the KYC norms prescribed by SEBI”*

(b) I note that the Enquiry Officer *inter alia* made the following observations with respect to this charge:

"6.4.0 With regard to introduction of accounts to BbOB Goregoan Branch, BbOB Worli Branch, BbOB Ahmedabad Branch etc., it is noted from the submission of KSBL that some of its employees introduced such accounts. Kary group assisted Key Operators in opening of bank accounts with BbOB Worli/Goregaon and Ahmedabad. In this regard, it is noted that Annexure-3 to the show cause notice is a letter of BbOB dated 7.3.2006, the contents of which bear testimony to the facts that many accounts were introduced by Kary. The said letter while referring to the accounts opened with the bank for the purpose of financing of IPO of Maruti Udyog Ltd., also state that all accounts were introduced by Kary Securities Limited and Kary Investor Services Limited signed by Mr. Vyomesh Pandya representing the company. It is important to note that the said letter further states that "it is understood that at the time of opening of the accounts, Mr. Vyomesh Pandya used to bring all the SB Account opening forms duly filled in. The signatures of the applicants were also filled in at the time of submission of the forms and none of the applicants were present in the bank for affixing their signature at the time of submission of the application." Further, vide letter dated March 4, 2006, IOB had forwarded copies of account opening forms along with KYC forms in respect of the following accounts:

- SB A/c no. 12150 - Roopal Naresbbhai Panchal and Devangi Dipakbbhai Panchal
- SB A/c no. 12140 - Roopal Naresbbhai Panchal and Devangi Dipakbbhai Panchal
- SB A/c no. 11954 - Roopal Naresbbhai Panchal and 50 others as per list
- SB A/c no. 12149 - Roopa Naresbbhai Panchal and Devangi Dipakbbhai Panchal
- SB A/c no. 12001 - Kantilal J Shah and Roopal Naresbbhai Panchal and 50 others as per list.
- SB A/c no. 12004 - Ketan Atul Doshi and 50 others as per list
- SB A/c no. 11406 - Panchal Dipakbbhai Jaswantlal and Panchal Devangi Dipakbbhai
- SB A/c no. 11407 - Devangi Dipak Panchal and Dipak Jaswantlal Panchal
- Current A/c no. 1008 - Steelart Engineering Pvt. Ltd.

6.4.1 The said account opening forms also contain a list of names of 50 applicants attached to the names of SB A/c No. 11954 - Roopal Naresbbhai Panchal. On perusal of the said documents, it is noted that the name of each of the said 50 applicants are mentioned which also bear the specimen signature of the said applicants. The said document is certified by an employee of KSBL who is stated to be the authorized signatory. The instances cited above are only few of many such instances where employees of KSBL introduced the bank accounts in large numbers.

6.4.2 Further, it is noted from the submissions of KSBL that the address seal of the Company or its associate entities were affixed on the forms. This also indicates that the said entities were aware of the activities of their employees. The fact that the employees of KSBL were actively introducing the accounts which in a way facilitated opening of large number of demat accounts which were used for applying in the IPOs.

....."

- (c) The noticee *inter alia* made the following submissions (*vide reply dated May 19, 2007*) with respect to the allegation that it had introduced bank accounts of the key operators :
- (i) KSBL denied that the Karvy group assisted the key operators in opening the bank accounts with BhOB.
 - (ii) It is factually incorrect to state that Mr. Pradeep Bhogle of KSBL, Mumbai was the introducer of several bank accounts with BhOB, Worli as the said person had introduced only a few accounts where requisite KYC documents including copy of PAN card were available.
 - (iii) It is denied that Mr. Pradeep Bhogle introduced many accounts at BhOB, Goregaon. From the seven bank account opening forms (*received along with pre-enquiry SCN dated September 22, 2006*), six accounts were introduced by one D.K.Katakia, who was one of the key operators.
 - (iv) As regards, the observation that Mr. Vyomesh Pandya was acting on behalf of KSL and KISL, it is submitted that only one sample bank account opening form pertaining to Hemal Hetal Parikh has been provided. On scrutiny of this form, it is observed that Mr. Vyomesh Pandya has signed as the introducer wherein the stamp of KSL has been affixed in the space provided for the address of the introducer. The account was opened in June 2003, where all the relevant KYC documents were provided including the copy of the PAN card of the account holder. The PAN details of the applicant were found to be genuine on verification from the website of Income Tax Department. Hemal Hetal Parikh held a demat account with the noticee since 2003, wherein required documents were provided towards KYC. No shares from the said account had been transferred to any afferent account or to the accounts of the Key Operators. Mr. Devi Dutt (bank official), in his statement had stated that there are not more than 4-5 bank accounts at BhOB, Ahmedabad. Based on this statement, the question of introducing large number of accounts by Vyomesh Pandya, Ahmedabad does not arise. Therefore, the observation that Vyomesh Pandya had introduced many bank accounts with BhOB, Ahmedabad, is incorrect.
 - (v) With respect to the observation made in regard to the BhOB letter dated March 7, 2006, it submitted that apart from the copy of one application form (*which was in the name of Hemal Hetal Parekh*) no copies of sample account opening forms have been provided. The account opening form of HemalHetal Parikh is valid in all respects. Though, at this stage it cannot be proved as to when the application form was signed, there is sufficient proof on record that the person so introduced by Mr. Vyomesh Pandya was genuine.

- (vi) The observation that Ashish Chiplar, Amos Baid and V.H. Bhatt have introduced several accounts in BhOB, Goregaon branch is factually incorrect.
- (vii) As regards the observation that the bank account of Mr. Doshi Devang was introduced by Ashish Chiplar and bears the stamp of KSBL, it was submitted that the address column of the introducer bears the stamp of KCL and not the stamp of KSBL as observed.
- (viii) The letter dated March 4, 2007 from Indian Overseas Bank ("IOB") suffers from the following factual inconsistencies:
 - a. While the letter stated that there were 37 saving accounts and all the said accounts contained 50 additional names, the bank had given copies of only 9 saving account opening forms. Further, out of the said 9 accounts, with respect to three saving accounts viz., A/c nos. 11954, 12001 and 12004 it has given the list of 50 additional names as the part of the account only. Therefore, there is an apparent contradiction in the contents of the letter.
 - b. The letter states that IOB had funded 3118 individual applicants and that KCL had certified that all 3118 individuals had demat accounts with it. Assuming that there were 37 saving accounts and each had 50 additional names, even then the total number of applications which could have been financed by IOB cannot exceed 1850. Therefore, it cannot be understood as to on what basis the bank stated that KCL had certified that all 3118 demat accounts were held with it. Further, there is no mention with regard to the documents pertaining to the savings accounts of the other 1268 (3118 - 1850) individuals to whom IOB have financed.
 - c. It is also not understood as to how the Enquiry Officer had presented the details of 50 additional names in respect of 3 saving accounts viz., 12140, 12149 and 12150 when the same does not appear in respect of the said savings accounts as per the bank's letter. The same also raises doubts as to the veracity and authenticity of the data relied upon.
 - d. Though it has been alleged that these accounts were introduced by KSBL, a close scrutiny of the documents clearly show that the KYC forms provided along with the account numbers 12140, 12149 and 12150 do not pertain to the said accounts but pertain to another account bearing no. 11983. KSBL cannot be held liable for the bank or the account holder using the KYC documents originally submitted for one account and subsequently used for opening other accounts.

- e. With respect to account no. 12004, the name has been subsequently changed to include the words "& 50 others" which was not the case in the first place.
- f. The forms cannot become the basis for drawing any conclusion for the following reason:
- The list of 50 accounts seems to be separate document as there is no basis for connecting the savings account opening form with the list containing 50 additional names. The main account opening form nowhere mentions that there is an annexure to it in the form of a list containing 50 additional names.
 - The unusual serial numbering on the list purported to be a part of main savings account opening form raises a question about its credibility. The starting serial numbers of the list are as follows: A/c no. 12150 – Sl. Nos. from 9101 to 9150; A/c no. 12149 – Sl. Nos from 9051 to 9100; A/c no. 12140 – Sl. Nos. from 3251 to 3300, which is extremely abnormal.
 - Only based on a rubber stamp of KSBL on a sheet of paper containing 50 names and signatures, it has been alleged that KSBL has introduced the said persons to the bank. The bank has failed to collect the required KYC documents pertaining to these individuals and failed to do physical verification to identify the genuineness of the applicants.
 - With respect to the purported stamp of KSBL along with signature, it is submitted that the signature in the list annexed do not tally with the signature of the person who introduced the main saving account holder. Nowhere it has been stated as to for what purpose the stamp has been fixed.
 - In the light of the findings in the Enquiry Report that even bank introduction letter have been found fabricated, there is also a possibility that the key operator might have himself prepared the document, affixed the stamp and given the same to the bank.
- g. The submissions of IOB cannot be taken on face value since its involvement with key operators in terms of opening bank accounts with additional 50 names without following the KYC requirements is quite evident and the bank has tried to shift the blame on KSBL. KSBL, additionally pointed out the following -

- The bank included 50 additional names of individuals who were not apparently related.
 - The bank has not collected the KYC documents [(Photographs, Proof of Identity (POI) and Proof of Address (POA)] of 50 additional persons.
 - The person who introduced the main savings account holder and the person who purportedly signed in the list of 50 additional names is different. The signature of the introducer on the account opening form and in the purported list differs significantly.
- h. The Enquiry Officer has referred to SB A/c no. 11954 and made observations on the same. However, copies of the documents were not made available to it. Further, sweeping generalisations have been made that *"instances cited above are only few of many such instances where employees of KSBL introduced the bank accounts in large numbers"* without any basis and documentary proof, simply based on the letter of the Bank.
- i. Simply because employees of KSBL had introduced the accounts and put the address or stamp of the company on forms, it cannot be concluded that the company was aware of the activities of the employees. Wherever accounts have been introduced by the employees, such accounts were supported by requisite KYC documents including copy of PAN card. Just because the employee of the company had introduced one saving account on the basis of KYC document and subsequent to the introduction, such person (*whose account was introduced by its employee*) has in connivance with the bank opened more accounts by adding names or by introducing others as brought out in the case of DhavalKatakia (*who had introduced several accounts after his account was opened with the bank*) KSBL cannot be alleged to have facilitated the opening of large number of bank accounts, which facilitated the large number of demat accounts as alleged.
- j. KSBL denied that it had in any manner facilitated the key operators to open many accounts. At the relevant time KSBL was not aware that the demat accounts opened through IPO sub brokers were benami/fictitious accounts and were opened for the purpose of cornering shares in the IPO. The alleged afferent accounts have been opened by IPO sub-brokers.
- k. There has been a substantial role of sub-brokers in opening demat accounts not only with KSBL (*in its capacity as a depository participant*) but also with various other DPs. The IPO sub-brokers used to market the public issues by procuring large number of

applications and the same is a widely prevalent market practice. KSBL has over 18,000 IPO sub-brokers and some of them, apart from procuring applications, had also procured demat accounts for the clients. Therefore, no adverse conclusions can be drawn against KSBL, simply because of the procurement of applications by such sub-brokers. Some of the entities alleged as key operators were registered as sub-brokers with itself and were procuring both IPO applications as well as demat applications.

- l. In retrospect, KSBL realises that some of the IPO sub-brokers who were the alleged key operators, have exploited the loopholes in the system and have used KSBL (*in its capacity as a depository participant*) as one of the DPs amongst others for carrying out their manipulative designs. The problem is a systemic one since the same is not peculiar to KSBL (*in its capacity as a depository participant*) alone but there were other DPs who have been exploited by the Key Operators.
- m. The number of accounts opened by KSBL (*in its capacity as a depository participant*) has to be viewed against the backdrop of the company's scale of operations and infrastructure. The company has invested and built up huge infrastructure and has also employed enough man power to cope with huge volumes in this business. There are occasions when the company has activated large number of accounts on a single day and those accounts did not pertain only to the accounts procured by the IPO sub-brokers. The IPO sub-brokers procure applications from various applicants on a daily basis and submit the same in bulk at the office of the DP. During submission, most IPO sub-brokers also capture the data in the required format and submit the same along with the account opening application forms. The process of collecting the data in the form of soft copy is resorted to by most of the DPs as the same facilitates easy upload and saves time. This process is followed to ensure that the demat accounts are opened and activated in the shortest span of time.
- n. Based on the assumption that the date of activation is also the date of receipt of application, the Enquiry Officer has erroneously come to a finding that large number of demat accounts were opened by the noticee on a single day. All the accounts were opened after following the prescribed procedure and after obtaining the requisite KYC documents.

(d) With respect to the allegation of introduction of bank accounts, the submissions made by the noticee during the personal hearing and reiterated in the Written Submissions dated April 20,2015 are reproduced below:

“Introduction of BhoBAccounts by KSBL:

(i) *As per SEBI Order, none of the bank accounts were introduced by KSBL. Finding is that KSL and KISL had introduced the alleged bank accounts. For the alleged introduction of bank accounts by KSL and KISL, KSBL cannot be penalised.*

(ii) *While recording adverse findings regarding introduction of bank accounts pertaining to BHOB, various bank account opening forms pertaining to 50795 series have been analysed by SEBI. Significantly, the limited number of bank account opening forms (17 Forms) which were made available by the Enquiry Officer to KSBL were suitably responded by KSBL and it was demonstrated that wherever the bank accounts were introduced, the persons were genuine and had requisite KYC documents.*

Further, of the 50795 series bank accounts, save and except the Bank account opening form of Bank account no 50795/001 of Hetal Parikh (which was fully explained by KSBL as having proper POA/POI documents etc.), no other form was made available to KSBL .

Strangely, Bank account no 50795/001 of Hetal Parikh (which was fully explained by KSBL as having proper POA/POI documents etc. has not been even adverted to by SEBI in the Order, and the adverse inferences have been recorded on the basis of Bank Account opening forms which were never made available to KSBL, in gross violation of principles of natural justice.

Definitely, SEBI cannot, in order to get over the proper explanation given by KSBL in respect of the bank account opening forms as made available to it, refer to or rely on some other bank account opening forms which were not made available to KSBL and draw adverse inferences.

In context of BHOB Bank Account No 50795 series, it has been observed that the said bank accounts were used for opening demat accounts in the month of June 2003 and such “demat accounts continued to be operation till November 15, 2005, though the corresponding bank account was closed on October 27, 2003”. There was no such finding/ basis recorded by the Enquiry Officer in his report. The said basis for drawing adverse inferences has surfaced for the first time in the SEBI Order, which is again in gross violation of principles of natural justice.

(iii) *It is also pertinent to mention here that KSBL, as a depository participant, will not be in a position to know if the bank account mentioned by the demat account holders is active or closed / inactive unless informed by the demat*

account holders. In any case, these bank account holders did not have any trading accounts with KSBL – Stock Broker and therefore it is impossible for KSBL as a stock broker to get the information about the status of the bank accounts.

- (iv) However, the fact is that the bank accounts continued to exist and remain operational and in fact various refund orders were encashed in the said bank accounts. At Pg. 330 to 339 – Vol II, KSBL has annexed copies of the refund orders encashed in the said bank accounts. Same also completely destroys the credibility of the statement of Mr. Devi Dutt, Chief Manager BHOB.
- (v) It appears that said finding is based on statement of Mr. Devi Dutt, Chief Manager BHOB. Same cannot now be relied on in light of SEBI's confirmation that no reliance will be placed on the same.
- (vi) Further, sweeping allegations were made that KSBL as a depository participant had opened demat accounts with the additional accounts added to bank account no. 50795 and that these additional bank accounts, based on which the demat accounts were opened, were introduced by none other than the entities of Karvy group.

It is submitted that, barring the account opening form of 50795/001 in the name of Hemali Parikh, account opening forms for no other bank account, allegedly to have been introduced by Karvy group were provided at any point of time during the Enquiry Proceedings for verification. With respect to the bank account opening form 50795/001 which was provided, the same was dealt with in the proceedings against KSBL as a depository participant and submissions were made that the bank account holder indeed had a depository account with Karvy which was opened based on a valid POI and POA documents. No reliance can be placed on documents which were never made available for inspection.

Introduction of IOB Accounts by KSBL :

- (i) The allegation regarding introduction of IOB accounts by KSBL was not a part of Enquiry Notice dated 22.9.2006 issued by the Enquiry Officer. Same will also be borne out by the perusal of the SCN issued by Enquiry officer. For the first time, the findings pertaining to IOB accounts surfaced in the Enquiry Report dated 15.3.2007. It may be noted that the allegation of introduction of accounts was made only on the basis of BhoB accounts and not on the basis of IOB accounts, which were neither referred to nor relied on in the Enquiry Notice.

- (ii) *The findings in the SEBI Order pertaining to alleged introduction of IOB accounts are contained in Paras 26 to 39. The findings are based on contents of IOB letter dated March 4, 2006, Four Account Opening Forms (A/c No- 12004, 12140, 12149, 12150), Submissions made by KSBL in Appeal No 92 of 2006.*
- (iii) *In so far as IOB letter dated March 4, 2006 is concerned, it is riddled with inconsistencies and cannot be relied upon for drawing any inferences. For instance :*
- (a) *The letter states that there were 37 savings accounts and all the said saving accounts contained 50 additional names. Whereas in contrast, IOB is stated to have given copies of only 9 savings accounts out of 37 accounts. Further, out of the said 9 accounts, only with respect to three savings accounts viz. 11954, 12001 & 12004, there a mention that a list of 50 additional names was existing. Thus, there is an apparent contradiction in the contents of IOB's letter.*
- (b) *The letter states that IOB had funded 3118 individual applicants and that KCL had certified that all the 3118 individuals had demat accounts with it. Assuming that the 37 savings accounts were there and each one had 50 additional names as contended by IOB even then the total number of applications which could have been financed by IOB cannot exceed 1850. Therefore, it is not understood as to on what basis IOB is stating that KCL had certified that all 3118 individuals had demat accounts being held with it.*
- (c) *In the letter, there is no mention with regard to the documents pertaining to the savings accounts of the other 1268 (3118 – 1850) individuals, to whom IOB have financed as stated in their letter.*
- (iv) *A sweeping statement has been made in the letter dated March 4, 2006 that there are 37 savings account with tail of 50 additional names and all the accounts have been introduced by KSBL. But it is not clear:*
- (a) *Whether SEBI has sought the details of 37 saving accounts with a tail of 50 additional names .*
- (b) *Whether SEBI has confronted the author of the letter as to how he has mentioned in Para 4 of the letter that there are 37 saving accounts with a tail of 50 additional names, and in the immediate next Para 5 he has stated that a tail of 50 additional names is tagged with only three savings bank account viz. 11954, 12001 & 12004.*
- (c) *Whether SEBI has confronted the author of the letter as to on what is Current Account No 1008- Steelart Engineering Pvt Ltd referred to in Para 5 of the letter . Surely same is not in the name of any Key Operator.*

- (v) *Strangely, SEBI has not provided the statement of IOB Official who has issued the said letter. KSBL is still in dark as to whether SEBI has recorded the statement of official of IOB who has issued the said letter (like in the case of Bbob wherein SEBI has recorded the statement of Mr. Devi Dutt), or not. If SEBI has recorded the same, then why has it not been made available. And if SEBI has not recorded the same, then why grave departure in the case of IOB vis-a-vis Bbob. Admittedly, the contents of letter dated March 4, 2006 and the Account Opening Forms which have been enclosed with the said letter, have been heavily relied upon by SEBI for drawing adverse inferences.*
- (vi) *In the circumstances, wherein the letter dated March 4, 2006 is fraught with inconsistencies and contains sweeping observations against KSBL, both the statement of the author of the letter and his cross examination becomes crucial and critical.*
- (vii) *Significantly, it may be pointed out that as per the letter dated March 4, 2006, the saving bank accounts 12140, 12149 & 12150 which have allegedly been introduced by KSBL, do not have a tail of 50 additional names. When IOB itself is stating that 50 additional names were annexed in respect of only the three saving accounts viz. 11954, 12001 & 12004, then it is not clear how it has been concluded in the SEBI Order that 50 additional names were annexed in respect of the three savings a/c. viz. 12140, 12149, 12150 also. In view thereof, especially contents of Para 5 of the letter, the whole finding in the SEBI Order that KSBL introduced accounts with a tail of 50 additional names collapses. Definitely SEBI cannot cherry pick the Para from the letter dated March 4, 2006 which suits its conclusions and debunk the Para which supports the contentions of KSBL and is incompatible with the allegations of SEBI.*
- (viii) *At Para 31 of SEBI Order, KSBL's submission that List of 50 persons is a separate document has been rejected and KSBL's version has been discounted and discarded merely because the set of forms was given by Bank. Same is completely untenable and unsustainable.*

The point which has been sorely missed is that both the Bank and the Key Operators are intimately connected with the opening of the bank accounts. Admittedly, IOB has opened bank accounts with additional 50 names, which is exceedingly abnormal and unprecedented and also financed the said 50 names in the IPOs. Further, Key Operator is the primary bank account holder and he cannot feign ignorance that he is not aware that tail of 50 names is added to his bank account and more so when Key Operator is seeking finance from IOB and IOB is religiously providing the same. Further, who would be beneficiary of such an arrangement is also quite evident. Key Operator gets finance and Bank gets interest and the same is a happy arrangement and suits the interest of both the parties.

Admittedly, IOB in its letter had mentioned that it had financed 3118 individuals whose names were attached as lists to various accounts allegedly to have been introduced by Kary group. It is a common practice and also a mandatory requirement that a bank, while sanctioning any loan, should collect documents such as loan application, POI, POA etc. from the loanees while sanctioning / disbursing the loan. Whether the bank has collected any such documents while disbursing the amounts and if it had, whether SEBI had sought those details / documents from the bank. If SEBI had not done, why has there been such a grave negligence in seeking the information about these individuals, when it had chosen to rely on such information provided by the bank.

In the circumstances, IOB's submission cannot be taken on the face value, since the facts reveal that its officials' intimate involvement with key operators in terms of opening bank accounts with additional 50 names is obvious. The question which begs an answer is as to how IOB in any unprecedented manner and in violation of all banking norms opened savings account with a tail of 50 additional names and financed the said 50 names in the IPOs. Further, having opened the bank accounts in violation of all norms, will it not be the endeavour of bank official to shirk the accountability/responsibility for opening half-baked bank accounts and saddle the blame on to others, since it suits him. Strange part is, SEBI has not bothered to investigate the veracity of the statements made by IOB, despite KSBL pointing out same to SEBI consistently over the last 10 years.

It is reiterated that merely because the documents were furnished by none other than the concerned banks, it cannot be suggested that documents are free from any doubts or contamination or that the banks have revealed or portrayed the correct picture to SEBI. There is a huge question mark on the conduct and role of the provider of the said documents i.e. the employees of the banks, on whose statements SEBI had relied upon heavily for making allegations against Karyy .

(ix) KSBL submits that the purported lists were not attached to these account opening forms but were introduced in the records at a later stage and the Key operators themselves have prepared the document and fraudulently affixed the stamp and given the same to the bank. Said view is also fortified by the following factors viz: (a) There is no reference to the purported list in the Savings bank account opening form; (b) The KYC documents in the case of savings bank account do not pertain to the said account but pertains to a different account number; (c) The names in the purported list are not numbered serially from Serial No.1, (d) There is no reference to any demat account numbers in the said list.

(x) At Para 30 of SEBI Order, Mayur Modi's Affidavit has been discarded, wherein he has denied the signatures in the lists of 50 names appended to the account opening forms pertaining to the savings bank account nos. 12140,

12149, 12150 and 12004. Mr. Mayur Modi has not disputed the signatures on the KYC form, since he had put his signatures, while introducing the bank account based on valid POI/POA documents, and he has accepted the same. Since he had not signed any of the purported list containing 50 names, he has disputed the signatures on these lists being alleged as his signatures. It is inexplicable as to why SEBI has not bothered to even question Mr. Mayur Modi or record his statement.

(xi) At Para 29(e) of SEBI Order, while recording adverse findings regarding introduction of bank accounts with IOB, SEBI has relied upon submission made by KSBL in SAT Appeal no 92 of 2006. Admittedly, nowhere in the SCN issued by the Enquiry Officer or the SCN issued by SEBI (i.e. the Enquiry Report), any reference has been made to the submissions made by KSBL in SAT Appeal no 92 of 2006. Same were never disclosed or relied upon or even remotely adverted to in the Enquiry proceedings. Reference to the said basis for recording adverse finding of introduction of bank account with IOB, is coming for the first time in the SEBI Order, which is patently in gross violation of principles of natural justice and vitiates the findings on this score. In any event, it is submitted that even the admissions are explainable and the same cannot be construed as conclusive evidence. The submissions in the said Appeal have been interpreted out of context. Even if the submissions in the said Appeal are treated as an admission, it is submitted that the same have been properly explained by KSBL and shown not to be an admission on the basis of evidence produced by KSBL before SEBI. It is pertinent to note that the submissions in the appeal were made at a time when none of the concerned documents had been shown or furnished to KSBL. It was taken on the assumption that the allegations of SEBI were correct. After examining the documents furnished subsequently to KSBL by SEBI, it was evident that KSBL had not certified the said list nor had the employee of KSBL signed the same. The critical fact that, when the submissions were made in the said Appeal at the relevant time, SEBI had not made available any documents to KSBL with regard to the charge of introduction of bank accounts containing 50 additional names, has been completely overlooked while drawing adverse inferences. In the circumstances the reliance placed by SEBI on the same is completely out of context.

(xii) At Para 31 of SEBI Order, while recording adverse findings regarding introduction of bank accounts with IOB and the introduction of the alleged list containing 50 names, it has been observed that "It is important to note that the names added to the bank accounts were in the same order as that in which the demat accounts were held with KSBL (in its capacity as a depository participant) and such details were privy to KSBL only."

Admittedly, the aforesaid basis for alleging that list containing 50 names was introduced by KSBL was never ever referred to or disclosed in the SCN issued by the Enquiry Officer or the SCN issued by SEBI (i.e. the Enquiry Report). Reference to the said basis for recording adverse finding of introduction of list containing 50 names, is coming

for the first time in the SEBI Order. Same is again patently in gross violation of principles of natural justice and vitiates the findings on this score.

However, it may be noted that the demat accounts of persons referred to in the purported "list of 50 persons" were opened through the IPO Sub broker (Grace Consultancy), who had procured demat account opening forms and requisite KYC documents along with the IPO application forms, and had submitted the demat account opening forms along with the soft copy of the data to KCL (who was the DP at the relevant time i.e. in 2004) for the purpose of opening demat accounts. The sequence of demat account numbers of the persons in the purported list of 50 persons was available with the IPO Sub Broker (Grace consultancy). Therefore, it cannot be concluded that "such details were privy to KSBL only".

Further, at the relevant time i.e. in March 2005 (the date of alleged introduction of savings accounts) KSBL was not the DP. Furthermore, the demat accounts of 50 persons were opened by IPO sub brokers with KCL way back in 2004 (i.e. a year prior to the alleged introduction). Therefore, it cannot be concluded that KSBL was privy to the demat account details, when it was not the DP at all. Also, KCL had to provide the demat account details to the demat account holders / IPO sub broker for the purpose of mentioning the same in the IPO application form, as without these details the application would not have been accepted. Therefore definitely, IPO Sub broker was privy to the demat account details since he had opened the demat accounts with KCL. In view thereof, the finding that "such details were privy to KSBL only" is fallacious.

(xiii) *At para 38 of the SEBI order it is mentioned that a stock broker is responsible for the actions of its sub-brokers while operating within its ambit and scope of work. We submit that it is essential that SEBI appreciates the difference between primary market activities and the secondary market activities. We submit that primary market sub-brokers are different from secondary market sub-brokers. Primary market sub-brokers who mainly facilitate clients to apply in primary market issuances (IPO's) through stock broker are not regulated, and it is only the secondary market sub-brokers who facilitate clients of the broker to deal in securities on the Exchange trading platform that are registered with SEBI as sub-brokers and it is only the secondary market sub-brokers for whose actions can a stock broker be held responsible."*

7. I have considered the charge of introduction of bank accounts by KSBL and the submissions made by it. With respect to this charge, I note that this allegation was levelled against KSBL-DP also and the proceeding in respect of KSBL-DP culminated in the passing of the SEBI Order dated January 28, 2014, wherein KSBL-DP was prohibited, for the reasons stated therein, from taking up any new

assignment (i.e., not to take up any new clients) for a period of 18 months. As KSBL-DP had already undergone such prohibition, there was no further penalty to be undergone. This Order against KSBL-DP has attained finality as no appeal was filed challenging the same. The aforesaid order dated January 28, 2014 had dealt with the charge of introduction of bank accounts by KSBL and it was observed *inter alia* therein that –

“..... On careful examination of the facts, I note that the introduction of the main bank accounts and the addition of 50 fictitious names to each account paved the way for opening of the aforesaid accounts. Karvy DP facilitated the opening of demat accounts for the additional fictitious names. Therefore, the above discussed conduct of Karvy DP and other entities of Karvy group can be said to have facilitated the key operators to procure IPO finance from the banks and hence, it had aided and abetted the key operators in cornering the shares in various IPOs”.

The noticee has contended that the BhOB accounts were introduced by KSL and KISL and that for such acts done by other Karvy entities, KSBL cannot be penalized. KSBL has also contended that bank account (50795/001) of Hetal Parikh was KYC compliant and SEBI has drawn adverse inferences on the basis of account opening forms which were never made available to it.

The noticee has also contended that the IOB letter dated March 04, 2006 (which referred a list of 9 accounts stated to be introduced by Karvy entities including KSBL) was fraught with inconsistencies and has doubted the veracity of such letter. In this regard, I note that elaborate observations and findings were made in the Order passed in respect of KSBL (DP). It is noted that documents pertaining to four IOB bank accounts viz., 12004, 12140, 12149 and 12150 where 50 additional names were added, were supplied to KSBL as samples. Out of the above, except account no. 12004 which was introduced by KCL, all the other three accounts were introduced by KSBL.

On perusal of the documents pertaining to the above sample bank accounts, it is seen that the 50 names added to each bank account number were sharing common surnames. The names added to the bank accounts were in the same order as that in which the demat accounts were held with KSBL (DP). It is seen that all the signatures in the list of 50 names appear to be made by one person. I also note that all the names contained in the list attached to the application forms (*for opening bank accounts*) had demat accounts with KSBL-DP and refer to the relevant observations made in respect of KSBL-DP vide SEBI Order dated January 28, 2014.

The noticee has stated that the practice followed by the banks of attaching 50 names to the bank accounts is exceedingly abnormal and unprecedented. In such a circumstance, the existence of even one such list bearing the stamp of KSBL is totally inconsistent with the possibility that KSBL was an innocent bystander and a victim.

The noticee has strenuously argued that the Banks were wrong in doing certain things, like not collecting KYC documents of afferent account holders. However, I reiterate that the present proceeding is in respect of an intermediary under SEBI regulations.

The noticee has also argued that simply because some employees of KSBL had introduced the accounts, it cannot be concluded that the company was aware of the activities of the employees. I am not inclined to give credence to this argument. The company has to be held responsible for the acts of the employees done on behalf of the company, based on the principal-agent relationship.

The noticee has contended that Mayur Modi's Affidavit has been discarded, wherein he has denied the signatures in the lists of 50 names appended to the account opening forms pertaining to the savings bank account nos. 12140, 12149, 12150 and 12004. KSBL further submitted that Mayur Modi has not disputed the signatures on the KYC form, since he had put his signatures, while introducing the bank account based on valid POI/POA documents, and he has accepted the same, whereas he has disputed the signatures on these lists being alleged as his signatures as he had not signed any of the purported list containing 50 names. KSBL also contended that it is inexplicable as to why SEBI has not bothered to even question Mr. Mayur Modi or record his statement. I note that having denied the signatures vide his affidavit, Mayur Modi would reiterate the same even if he was asked for a statement before SEBI. Therefore, questioning Mayur Modi regarding his signatures and recording his statement may not achieve anything new. In this regard, conclusions need to be drawn on the whole set of facts, documents and circumstances of the case. Therefore, viewing an act or event or document in an isolated manner would not present the matter in the correct perspective. I also note that in the Order dated January 28, 2014 passed against KSBL-DP, SEBI has observed the following:

*"It is strange to note that the list of 50 names attached with the account opening form for the bank account bearing no. 12140 bear a common surname i.e. **"SETH"**, starting from **'SURESH SETH'** and ending with **'ADITI***

SETH', and that the signatures of these 50 are in English, Hindi and Gujarati and appear to have been signed by the same person in similar manner. Further, the signature of the representative of KSBL on the main bank account introduction column and that in the attached list of 50 names of one Mr. Mayur Modi. On comparing the signature of Mayur Modi in the KYC form with respect to account no. 12140 and the signature present in the list of 50 names attached to that account, it is difficult to say that the signatures are different. Further, the same Mayur Modi had signed on the introduction column (in the account opening form with respect to bank account no. 12004 with IOB) on behalf of both KCL (now Karvy DP) and KSBL. I have perused the affidavit dated June 02, 2007 of Mayur Modi filed before SEBI, wherein he has denied that the signatures in the lists of 50 names appended to the account opening forms pertaining to the savings bank account nos. 12140, 12149, 12150 and 12004 are not his. I have also perused the copy of his PAN card annexed with the affidavit and the signature contained therein and the signatures in the lists containing the 50 names. On perusal, it can be said that in all these the signatures are done by Mayur Modi with the normal variations in signatures of a person. It is important to bear in mind that these 50 names in the attached list had their demat accounts with Karvy DP in the same sequence (as that in the bank account opening form), the demat accounts starting with BOID IN300394 13130266 - 'SURESH SETH' and ending with BOID IN300394 13130776 - 'ADITI SETH', all of which were opened on January 05, 2004."

In view of the facts and circumstances of the case, I would reiterate the same finding herein also and do not find merit in the above contentions made by KSBL.

From the submissions of the noticee, it is noted that it has not denied outrightly the involvement of any of the entities of the Karvy group. It has taken technical arguments to controvert the allegations. It is seen from the above observations that the noticee has introduced the entities in the list of 50 (fictitious) names and bank accounts were opened for such names. Opening of bank accounts enabled the non-existent persons to avail finance from KCL/Banks for applying in the IPOs.

KSBL has also contended that the charge of introduction of IOB accounts was not alleged in the SCN dated September 22, 2006 and came out for the first time in the Enquiry Report. However, I note that adequate opportunity was afforded to the noticee to make its submissions on such observations of the Enquiry Officer and therefore no prejudice is caused to the noticee in that regard.

In view of the foregoing, I hereby conclude that the noticee was responsible for introduction of bank accounts with list of 50 fictitious names.

8. Another allegation against the noticee is that it had facilitated key operators and financiers including Purshottam Bhudwani and Manoj Seksaria to sell shares which were cornered by them in the IPOs in the securities market. The SCN alleged that -

“71. Further it is alleged that KSBL (in the capacity of stock broker) had facilitated key operators and financiers including Purshottam Bhudwani and Manoj Seksaria to sell shares which were cornered by them in the IPOs in the market by its various actions as mentioned KSBL violated the provisions of section 12A of SEBI Act, 1992 and Regulation 3 and 4 of the SEBI(PFUTP) Regulations 2003. Besides it is also alleged that KSBL in the capacity of depository participants aided and abetted and facilitated the key operators in furtherance of their objective of cornering shares with the active help of its broking arm account on account which it alleged to have violated the provisions of Clause A(2) of the code of conduct as prescribed in schedule II under Regulation 7 of the SEBI(Stock Brokers & Sub Brokers) Regulations, 1993.”

With respect to this charge, the Enquiry Officer had observed that

- a) the noticee had sold the shares on behalf of Purshottam Bhudwani and Manoj Seksaria, knowing that the same were cornered by such key operators.
- b) 5,32,000 shares were cornered by Purshottam Bhudwani and Manoj Seksaria each, in IDFC IPO.
- c) Out of the said quantity, Manoj Seksaria sold 4,77,500 shares through the noticee at the rate of ₹61.67/- on the listing day i.e. August 12, 2005. Further, Purshottam Bhudwani sold 5,00,000 shares on August 12, 2005 through the noticee at the rate of ₹61.25/-.
- d) Both the said key operators had made huge profits out of such transactions.
- e) Mr. Purshottam Bhudwani had received (*in his account no. 0602100001225 maintained with HDFC Bank Ltd., Fort Branch*) a sum of ₹3,05,76,060.80/- from the noticee.

The noticee made the following submissions (as reproduced below) in respect of this charge during the personal hearing and reiterated in the Written Submissions dated April 20, 2015:

“Sale of shares (which were cornered by the key operators in the IPOs) through KSBL

- (i) *As per SEBI order the shares sold were substantial and KSBL as a registered intermediary, cannot be ignorant of the facts that such shares were allotted in the IPOs at the relevant period; and its clients (i.e. the key*

operators), as retail category allottees, would not be allotted such huge quantities in the IPOs and KSBL should have been alerted by such factors.

- (ii) *Admittedly, the basis of allegation in the Enquiry SCN or Enquiry Report was never that KSBL as a registered intermediary, cannot be ignorant of the facts that such shares were allotted in the IPOs at the relevant period; and its clients (i.e. the key operators), as retail category allottees, would not be allotted such huge quantities in the IPOs and KSBL should have been alerted by such factors. The said basis has surfaced for the first time in the SEBI Order, which is in gross violation of principles of natural justice.*

At the relevant time, there was no embargo on off market transfer of shares post allotment of shares in the IPO and pre -listing of shares on the exchanges. Allotment in the IDFC IPO took place on August 5, 2005 and the shares were listed on August 12, 2005. During the period August 5, 2005 to August 12, 2005, there was no embargo on transfer of shares. Therefore, to suggest that KSBL's dealer while executing the sale transaction in the secondary market should have got alerted that how these many shares were being sold by Purshottam Budhwani or Manoj Seksaria, is absurd. Significantly, off market transfer of shares post allotment and pre listing was a common phenomenon at the relevant time. Same will also be borne out by the Statement enclosed as Annexure 1 (which was submitted by us during the course of hearing) prepared on the basis of demat accounts in which shares were allotted but shareholding was not appearing as on the date of listing of the securities(in respect of IDFC IPO). On a perusal of this statement can be seen in the case of all the syndicate / sub-syndicate members the shares are allotted to a certain number applicants in their demat accounts on the allotment date and some of these applicants/ demat account holders transfer out the shares to other persons/entities before the listing date due to which their holding in the respective scrip is NIL. This process is basically consolidation of shares into lesser number of demat accounts and allottees/persons. This submission is made just to substantiate that in the era where off-market transactions in the respective scrip was permitted between the allotment date and the listing date, such consolidation of shares into lesser number of demat accounts was in vogue and there was nothing untoward or alarming. It is only much later in 2006 that SEBI brought in regulatory changes which directed the enablement of ISIN on the depository system only on the listing date.

- (iii) *Findings in the para are based on the presumption that at the relevant time when KSBL had executed the sell orders for the key operators on August 12 2005, it was also a DP. Same is completely contrary to factual position on record. IDFC IPO took place in July 2005, when KCL was a DP. KSBL, as a Stock broker, had no role to play in opening of the demat accounts pertaining to Purshottam Budhwani & Manoj Seksaria. Further, even when the shares allotted in IDFC were credited to the demat accounts of allottees, KCL was the DP. Furthermore, when the shares of IDFC were transferred by Purshottam Budhwani & Manoj Sakseria from various alleged fictitious accounts to their own demat accounts in off market, KCL was the DP. Therefore, when the shares were delivered by the said Key Operators from their own demat accounts for sale to KSBL, there was no occasion for KSBL to suspect about the antecedents of the shares sold (i.e. the shares were illegally cornered) by Purshottam Budhwani & Manoj Sakseria.*

- (iv) *While selling the shares, the broker is concerned to the limited extent that the shares sold are being delivered from the client's demat account only, which in the matter under reference the clients had delivered. How the shares have been procured by the broker's client in his demat account is not the concern of the stock broker. The dealer while executing the transaction only verifies whether sufficient quantity of shares are available with the client for delivering the same for pay-in to the stock exchange.*
- (v) *Significantly, it is not the case that KSBL as a stock broker had either introduced the bank accounts of the said Key Operators, viz. Purshottam Budhwani or Manoj Sakseria or funded them. Merely based on sale transaction pertaining to IDFC shares, adverse inferences have been drawn. It may be noted KSBL's nexus has been alleged with various Key Operators and in context of various IPOs, but the charge of sale is limited to IDFC IPO only.*
- (vi) *Point which has been missed out is that for opening the alleged fictitious demat accounts and the subsequent off market transfers by KCL- DP, SEBI has already penalised KSBL as a DP. Therefore, for the same transaction, there is no warrant for penalising KSBL - Stock Broker, who had sold the shares in the Secondary market in the ordinary course without being aware of the antecedents of the shares i.e. they are cornered shares as alleged.*
- (vii) *Pertinently, it may be noted that in the similar circumstances, wherein KSBL had sold 57,500 shares of NTPC on behalf of DB Mehta - the Key Operator (who is alleged to have opened large number of fictitious / benami accounts and had got the shares transferred to his demat account from various fictitious / benami accounts), the Adjudicating officer SEBI vide his Order dated February 13, 2008 had not found any fault with KSBL and had in fact concluded that KSBL "was acting in the capacity as a stock broker and received the said shares of NTPC as margin towards execution of sell order of the client DB Mehta. In view of the same it cannot be concluded that transfer of 57,500 shares of NTPC on November 5, 2004 was in violation of Section 12 A of SEBI Act and regulations 3, 4, and 6 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations 1995 and regulations 3 & 4 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations 2003 and accordingly the present adjudication proceedings against the noticee is disposed off."*

Significantly, the very same charge pertaining to the sale transaction is also contained in Enquiry Notice. Same will be evident from Para 67 of Enquiry SCN.

- (viii) *It is incomprehensible as to how when it comes to sale transaction of Manoj Sakseria & Purshottam Budhwani, SEBI is not accepting the version of KSBL and when it comes to the sale transaction on behalf of D B Mehta, SEBI is accepting the version of KSBL. Fact is in both the cases KSBL was acting as a broker on behalf of the clients and had nothing to do with the alleged cornering of the shares and also had no knowledge of any alleged cornering of the shares. The activities which have transpired in the Primary market cannot be mixed up with the activities of the Secondary market. KSBL operating in Secondary market, while selling the shares, cannot be*

saddled with the knowledge of alleged cornering (in which KSBL had no role to play) which has taken place in the Primary market?

9. I have considered the observations/findings of the Enquiry Officer and the submissions of the noticee made in this regard.

(a) The sale of shares by the noticee on behalf of Purshottam Bhudwani and Manoj Seksaria is a fact and has not been disputed. The noticee has made submissions to show that sale of shares were done in the normal course of business and there was no occasion to doubt the same. In this regard, I note that the sale of shares cannot be seen as an act in isolation and it has to be viewed in the light of activities of other Karvy Group entities and how these shares were acquired in the first place and the following observations made in the SEBI Order dated January 28, 2014 in respect of KSBL-DP may be referred here :

“In my considered opinion, if Karvy DP was working in normal circumstances, it ought to have raised certain suspicion on such transfers/ accumulations in the demat account of the key operators. It is for these purposes that market intermediaries are given specific responsible roles in the securities market. Therefore, the detailed discussions in the paragraphs above only demonstrate the collusion of Karvy DP with the key operators. I note that the market intermediaries act as first line of regulator in the securities market and it is their primary responsibility to keep an eye on all what happens in its domain. A regulator expects that an intermediary would make every effort in order to make the market more safe and secure for the investors, and thus eliminate fraud or unfair practice from the market.

15. *I note that the Karvy group as a whole appeared to have favoured an extremely aggressive approach to business leading to their direct involvement in the IPO manipulation. Karvy DP has tried to disown the responsibility. I note that the entire case revolves around the unusual business practices adopted by Karvy group entities. The only way Karvy DP could have been absolved of all responsibilities, would be by proving that it had nothing to do with the key operators, opening of bank accounts, refunds etc. It is a binary situation; whether Karvy DP was associated with the group of wrong doers or not. If it was associated, then the shortcomings and discrepancies in documentation mentioned by Karvy DP does not help in it getting a clean chit or even a benefit of doubt. Karvy DP has tried to distance itself from the activities of the other Karvy entities and the key operators, however, the discussion above makes it clear that the operations of the Karvy group entities were supplementary to their roles and complementary to each other. This gives a strong*

presumption that Karvy group entities had acted in close coordination and the whole group should be viewed as one, irrespective of the separate legal identity of different entities.

16. *I note that the shares meant for subscription in the retail category have been cornered in the IPOs by the key operators which included the IPO sub-brokers of Karvy DP. The said act was prejudicial to the interests of the investors and the retail applicants in such IPOs. After cornering the shares meant for retail investors, the key operators sold them to make large profits. I note that in the entire chain of events, the Karvy group entities were involved, which clearly suggest that all of them had acted in concert and facilitated cornering of the shares and by no stretch of imagination can the role of Karvy DP be considered independent to the scheme of cornering of shares. Karvy DP has submitted that the IPO sub-brokers were the ones who opened the afferent accounts and that it was not aware that such demat accounts were benami/fictitious accounts and opened for the purpose of cornering shares in the IPO. Even if, I were to accept the said submission of Karvy DP, the fact that would remain is that it had turned a blind eye to the unusual situation where names and surnames appear in hundreds of accounts with mathematical regularity and points to much more than merely not exercising proper diligence and prudence.”*

(b) Given the fact that KSBL-DP facilitated the opening of numerous afferent accounts (demat account of fictitious and benami names), KCL financing the IPOs, Karvy group entities including KSBL introducing bank accounts of fictitious/benami persons which enabled them to avail finance from the banks (BhOB/IOB), KCPL acting as registrar in IPOs, selling of shares cornered by key operators through the stock broking arm of Karvy i.e., KSBL, leads one to infer that the sale of shares cannot be in the normal course but was done in pursuance of the effort of the key operators to sell the cornered retail portion and thereby reap profits. Manoj Seksaria and Purshottam Bhudwani were the key operators who had abused the system and the IPO process. They were also the noticee’s clients and IPO sub-brokers during the relevant point of time. The preponderance of probability of this case would never allow a conscious mind to view the 'sale transaction' as a normal transaction done by a stock broker in respect of its client.

(c) The contention of the noticee is that the fact of trading by such key operators through it cannot lead to an inference that it was aware that they were selling shares that were cornered. KSBL has also

submitted that when shares were delivered by the key operators from their own demat accounts for sale to KSBL, there was no occasion for KSBL to suspect the antecedents of the shares that were sold.

(d) The noticee has contended that SEBI did not find fault when it sold shares on behalf of D.B.Mehta who was an alleged key operator. In this regard, I note that the SCN dated September 22, 2006 issued to the noticee had alleged that the noticee had financed D. B. Mehta, a key operator, for making 575 applications in the IPO of NTPC. D.B.Mehta was found to have transferred 57,500 shares to the demat account of KSBL. In respect of this charge in the pre-enquiry SCN, the Enquiry Officer observed the following;

"5.1 It is noted from the submissions of KSBL that it had not financed Shri D.B. Mehta as alleged in the show cause notice. It is further noted from the submissions of KSBL that it was in respect of the pay in obligations of its client Shri D.B. Mehta that the shares were transferred to its account. In this regard, it is pertinent to note that in respect of the alleged role of KSBL as a financier, separate adjudication proceedings have been initiated against KSBL. In view of the same, no adverse finding is recorded in this enquiry as the said allegation of acting as a financier is being inquired into in the adjudication proceedings against KSBL."

I have considered the above contention of the noticee and I am of the view that the findings were made in respect of the charge against noticee in respect of it acting as a financier. It appears that the case has been viewed against the charge that KSBL financed DB Mehta and not sale of shares of a key operator.

(e) Considering the totality of the facts and circumstance of the IPO irregularities case, it becomes very difficult to accept the version of the case as contended by the noticee. It becomes necessary and important to relate the 'sale transaction' executed by the noticee for key operators including Purshottam Bhudwani and Manoj Seksaria with the events of the case that unfolded which ultimately resulted in the key operators selling the cornered IPO shares in the market for huge profits.

10. During the personal hearing, the noticee submitted that 'bidding of IPO applications by KSBL' was not a charge in the SCN. The noticee has made the following submissions:

"....., there was no charge that KSBL had, as a Syndicate Member, collected the IPO application forms enclosing payment instruments from not from the original applicants but from key operators."

“there was no charge that KSBL had, as a Syndicate Member, accepted applications with cheques / DDs coming from the key operators, and had accommodated the key operators in making fictitious applications for cornering shares in the IPOs. Further, there was no allegation that KSBL had bid fictitious applications on behalf of PurshottamBudhwani and ManojSakseria.

the individual IPO applicants were having bank accounts with HDFC Bank and were joint account holders with ManojSakseria or PurshottamBudhwani and that there is no law which mandates that the IPO applicant has to enclose cheque drawn from his own account only. The IPO applicant can always enclose the cheque from the account of a third party. The same is an accepted market practice.

The role of a Syndicate Member while bidding the applications is to punch in the data (viz. application no, DP ID, Client ID, name of the investor, cheque no etc) in a common platform for the purpose of registration of his intention to make an application in the IPO at a desired price.

All the IPO Applicants had valid demat accounts with KCL as a DP and bank account with HDFC bank. POA/POI documents in respect of 10 of the IPO applicants, on illustrative basis, are annexed Thus, none of the accounts are fictitious as alleged. Persons holding the bank / demat accounts exist.

Significantly, none of the bank accounts of these IPO applicants have been introduced by KSBL.

Inferences in the para are qua KSBL in its capacity as a Syndicate member and not as a Secondary market stock broker.”

I have considered such submissions. Though bidding of IPO applications is not an allegation in the SCN, it is a fact that KSBL acted as a syndicate member in the IPOs.

11. The noticee also made submissions vide reply dated May 19, 2007 *inter alia* contending that it did not have nexus with the key operators and was not aware about the activities of KCL and KCPL. As regards the observations of the enquiry officer with respect to "*activities of the Karvy group entities in the manipulation in the matter*", the noticee *inter alia* submitted that Karvy group maintained arm's length between them. I have considered the contention in the light of the events of the IPO irregularity and note the following:

(a) The fact that IPO (where cornering of shares were done by key operators) applications were procured by KSBL/its IPO sub-brokers/key operators like Purshottam Bhudwani and Manoj Seksaria cannot be overlooked though the same was not a specific charge either in the pre-enquiry SCN or the Enquiry Report. Considering the above and the roles played by KSBL-DP and KCPL in the IPOs and

the same being found in the respective SEBI Orders , it can be concluded that KSBL had a role in the opening of bank accounts with additional names without supporting KYCs, procuring and bidding of IPO applications, sale of shares (that were cornered in IPOs by key operators) and the preponderance of probability suggests that KSBL has accommodated the key operators in their fraudulent act in cornering shares in IPOs and thereby benefitting by selling them in the market. The presence of KSBL as a DP, procuring and bidding IPO applications and sale of shares especially on behalf of two key operators-Purshottam Bhudwani and Manoj Seksaria is too much of a coincidence to take a view that the noticee, as a stock broker, was not aware of the events that happened during the IPO manipulation. It can be said that various entities of the Karvy Group including KSBL-DP, KCPL and the noticee played their roles and supplemented and complement each other.

(b) The noticee is a depository participant (having taken over from KCL) and also a stock broker. Its role as a DP in the IPO irregularities have been explained in the SEBI Order dated January 28, 2014 passed in respect of Karvy-DP. I also note the following observations from the Order dated passed in respect of Karvy-DP:

"The manner in which the funding was done, even after the closure of the issue and the amount of loan extended to key operators like Purshottam Bhudwani and Manoj Seksaria hints that Karvy DP was aware that large number of fictitious applications have been made by the key operators. I agree with the findings of the Enquiry Officer that the extent of involvement of Karvy DP and its associate entities in the whole gamut of the IPO process indicate that on many instances, the activities of Karvy DP and its associates were complementary and supporting each other. Similarly, Karvy DP at the relevant point of time had implicit arrangements with certain banks like BbOB for offering finance to the key operators who also happened to be its IPO sub-brokers. Large scale financing was extended by KCL to the said IPO sub-brokers. The various Karvy group entities, i.e., KCL, KSBL, Karvy Investor Services and Karvy Securities Limited had introduced the said key operators to open bank accounts. Further, KCPL issued consolidated refund orders and KSBL, the broking arm of Karvy group sold the shares for the key operators.

.....

I have considered the submissions of Karvy DP in the light of the discussions in the earlier paragraphs. From the bank account opening forms, I note that a single person has signed on behalf of KCL and KSBL. Considering the fact that the bank accounts, as discussed above, were introduced by one of the Karvy group entities and that subsequently 50 fictitious names were added to each of these accounts, there is a definite conclusion that Karvy DP as a registered intermediary was acting in concert with other Karvy group entities. I note that KCL had provided finance to thousands of such similar set of fictitious names. KSBL (the stock broking arm of Karvy group) had entered the bids for these applicants through its system and KCL/ Karvy DP facilitated off-market transfer of the

shares allotted (to these applicants) to key operators. Further, KCPL issued consolidated refund orders to the same set of entities. In addition to this, I note that KSBL had bid the applications without obtaining the application money and further, the money was transferred by RTGS in certain instances on subsequent dates. The money transferred by RTGS was that funded by KCL. It is also found that KCPL being the RTI of the issue had issued a consolidated refund in respect of such applicants. Also, Karvy DP facilitated transfer of the IPO shares from the demat accounts of the fictitious/ benami entities to the demat accounts of the key operators by supplying pre-printed DISs.

From the entire sequence of events, brought out in the previous paragraphs, the only logical conclusion is that each one of Karvy group entity had a pre-assigned role and that all had knowledge about each other's role. Thus, I conclude that the Karvy group entities has not maintained arm's length distance between its different businesses in the securities market, starting with the DP, financier, RTI and ending with the stock broker. Rather, the chain of events and the manner in which they have occurred, demonstrate that all these entities were hand in glove with each other and were supplementing the activities of each other. "

(c) In the words of Hon'ble SAT in the matter of Ketan Parekh vs. SEBI, whether a transaction has been executed with intention to manipulate the market or defeat the mechanism will depend upon the intention of the parties which could be inferred from attending circumstances as direct evidence may not be available. In view of the above, the other submissions made by the noticee that it did not collude with the key operators and was not aware of the manipulations are not plausible.

(d) The standard of proof in the cases of irregularities committed by an intermediary in a quasi-judicial proceedings is fundamentally different from the standard of proof required in case of criminal charges pressed against an individual. In the latter case, inconsistencies in the data/information given by the prosecution might be fatal and lead to acquittal. However, for an intermediary to say that he was not involved in the shenanigans of manipulators, it will be necessary to assert that the intermediary had absolutely nothing to do with the wrong doings. Being slightly involved is no defence. An intermediary cannot be good in parts.

(e) KSBL, by no stretch of imagination was an innocent bystander who became a victim of the machinations of the key operators. Considering the facts and circumstances of the case in its totality, I hereby find the noticee of contravening the provisions of section 12A(a), (b) and (c) of the SEBI Act, regulations 3 and 4 of the PFUTP Regulations and Clauses A(1), (3) and (4) of the Code of Conduct for stock brokers prescribed under the Stock Brokers Regulations.

12. I also note that the noticee made the following submissions to highlight the following regulatory changes that were made in order to plug the loopholes:

“Opening of Demat Accounts:

- (i) *Permanent Account Number (“PAN”) has been mandatory for opening of demat accounts w.e.f. March 31, 2006. DPs are required to cross-check the particulars of PAN card with the details appearing on the website of the Income Tax Department. This would ensure that there is sufficient proof of the existence of the applicant.*
- (ii) *In addition to requirement of procuring PAN, ‘in-person verification’ of beneficial owners has been made mandatory since March 16, 2007.*
- (iii) *100% verification of the account opening documents by a concurrent auditor has been made mandatory to ensure that independent assessment of such documentation in relation to each application made to the DP.*
- (iv) *Depositories have developed ‘de-dupe’ softwares to better detect demat accounts having five or more demat accounts with same name or address or bank name and bank account number or PAN etc. This is aimed at ensuring minimizing and thereby mitigating the symptom of ‘multiple applications’.*

IPO Processing:

- (i) *Depositories have been advised to activate the ISIN only on the date of commencement of trading on the stock exchanges, so as to avoid off-market transfers before listing of scrips.*
- (ii) *Number of applications which can be made in the IPOs against a single bank account has been restricted to five applications per bank account in ASBA.*
- (iii) *Validation of data in IPO applications is mandatorily required to be made with the depository ID and client ID of the applicant.*
- (iv) *Refund in the IPOs happens through electronic credit (NECS/ECS/RTGS) unlike in the physical mode earlier. {Ref:- SEBI’s Circular No. SEBI/MRD/DEP/Cir-2/06 dated -January 19, 2006 (Page- 460/Vol II) & NSDL’s Circular No. NSDL/POLICY/2006/0007, dated-March 3, 2006(Page-461/Vol II)}*

13. The noticee has buttressed the submission that the manner of opening of afferent demat accounts cannot happen now in view of PAN being made mandatory and the verification of the existence of an account holder. It is also submitted that off-market transfer of IPO allotted shares cannot be made prior to the listing date and also the validation of data in IPO application with that of DP client details. The steps taken by the regulator to prevent abuse in future cannot be a defence for an intermediary.

14. After having arrived at the violation committed by the noticee, the further step is to determine the nature of penalty that would commensurate with the violations as found against the noticee in the light of the observations made above. The Enquiry Officer has recommended the suspension of noticee’s registration as a stock broker for a period of three months. This recommendation was made vide Enquiry Report of the year 2006.

(a) With respect to the penalty, the noticee has submitted that in the light of charges against it, it would be evident that the same are related to Primary market activities. The noticee also submitted that ‘..... it may be appreciated that a Stock Broker’s activities can be broadly classified into two areas, viz. Primary market activities and Secondary market activities. The Primary market activities inter alia include acting as a Syndicate/ Sub Syndicate Member in the IPO’s for procuring IPO application forms and bidding the same. The Secondary market activities inter alia include executing buy and sell trades on behalf of the clients registered directly or clients registered through SEBI registered Sub- Brokers.’”

(b) The noticee further submitted “The entire investigation of SEBI in the impugned proceedings have been focused and centred on the abuse of the IPO process, which is basically a Primary market activity. Even the thrust of the allegations in the SEBI Order (viz. Introduction of bank accounts, Connection with IPO Sub brokers/ Key Operators, Bidding of the IPO applications as a Syndicate Member, Sale of shares cornered in the IPO etc.) are in context of Primary market activities carried out by KSBL during the relevant period. Charges have no nexus with the Secondary market activity carried out by KSBL as a stock broker.” With respect to the direction issued against KSBL vide SEBI Order dated March 14, 2014, the noticee submitted that "While issuing direction of prohibiting KSBL from taking up any new assignment or contract or launch a new scheme (i.e. not to take new clients/ customers) for a period of 6 months in respect of its business as a stock broker, no distinction has been made with regard to activities undertaken by KSBL, in Primary Market and Secondary market. Since the findings in the SEBI order pertained to activities in the Primary Market, the directions should have been limited and restricted to activities undertaken by KSBL in Primary Market alone (i.e. as a Syndicate Member). The directions should not have included within its sweep activities undertaken by KSBL as a stock broker in the Secondary market."

(c) The noticee also made the following submissions to highlight the fact that it has already suffered enough penalty on account of the proceedings against it.

“The penalty already suffered by KSBL should suffice and no further regulatory intervention is required in the facts of the case. In this context following be noted that:

(i) *As a result of these proceedings, which have been initiated in 2006 close to a decade ago, Kavya, as a Group has already suffered and has been penalized disproportionately. There have been penalties imposed against various entities, depending on the nature of business activity. The suffering of the entire group, and the beating that the brand ‘Kavya’ took, cannot be measured only by the penalties imposed, which we submit were disproportionate to the loss suffered, but also by the consequential difficulties suffered by the other related businesses in the group. The Kavya group has*

been subjected to a plethora of other proceedings, both civil and criminal, when SEBI had lodged a complaint against Karvy before other courts and other agencies, on the same set of facts. There have been innumerable law enforcement and other agencies which have investigated our senior managers and our officers, and the suffering, both on official and personal levels, have been severe, and have broken the back, in both, the actual sense and the literary sense of the word, of the Karvy group. It is a miracle that the organisation has survived, which is not because of the determination of the management and the employees of the company, which has also been considerable, but because of the yeoman services rendered by the group in every nook and corner of the country, to the investors, especially the retail investors, and also the other members of the public. It is the common man in the country whose goodwill has ensured that this organisation has survived.

- (ii) It will also be appropriate to submit that the expertise of the Karvy group was even solicited by the Government of India, Ministry of Disinvestment, when there were major problems in the disinvestment processes pertaining to ONGC. Similarly, when Karvy Computershare was serving the ban on taking new assignments by SEBI, upon a request made by a reputed investment banker, coupled with the consent of SEBI, we also undertook to help and complete the process in the IPO of Idea Cellular when the existing registrar could not rise to the occasion. It is pertinent to submit that these multiple proceedings have impacted further expansion plans, new ventures, and have resulted in the top management and the key personnel of the group focusing and attending to the pending proceedings, rather than focusing on enhancement of investor services, business development and future initiatives. The business activities of the Karvy group have been severely hamstrung by the pendency of the proceedings and the concomitant uncertainty attached with it.*
- (iii) As a result of multiple proceedings and the embargo's imposed on Karvy and consequentially, KSBL, coupled with the adverse media publicity as submitted earlier, the image was severely dented, which has resulted in the loss of reputation and business opportunity. In addition to the proceedings having impacted our business plans, restricting diversification into new ventures, etc., these have also disqualified us from working for, or bidding for work pertaining to various segments of the government, and also of SEBI. The brand image of the organisation having taken a beating, the consequential loss of reputation and business opportunities have been huge. Some opportunities not pertaining to the domestic market, have also taken at least thrice the normal time taken, apart from extensive explanations and submissions made at various levels. The number of instances where the Chairman of the company himself had to accompany the senior management for clarifying the status to new customers, in view of the clarifications sought by potential clients, have been innumerable, and all this has resulted into the organisation losing its status. It would not be out of place to submit that in the years 2004-05 and 2005-06, the group companies of Karvy were the largest registrar in the country, the largest non-bank DP in the country, the largest distributor of various IPOs, especially among the retail, apart from being among the top three secondary market brokers, and among one of those which had once of the largest number of retail clientele in this country.*

- (iv) *KSBL, as an entity, has already suffered restraint on buying, selling or dealing in its proprietary account for a period of 14.5 months (i.e from April 27, 2006 to July 4, 2007). Therefore it has not been in a position to invest or transact in securities in its proprietary account for a period of over 14.5 months, resulting in, a loss of opportunity during a bullish market period.*
- (v) *Despite some of these activities being distinct and separate, for a non-bank stock broker, there is a necessity to function and undertake activities in more than one segment. Simultaneously KSBL, as a depository participant had already suffered a ban of over 19 months. We submit that the consequent impact on the broking business on account of this ban has been tremendous as (a) not a single on-line broking account could be opened, and (b) most investors would not choose to open a broking account when the service provider does not provide a DP platform. It is absolutely necessary to make a mention of this only to state that the ban on opening new accounts as far as the DP business is concerned, has actually impacted the KSBL's broking business, and the slide and the downfall, as far as the market share and leadership position are concerned,, started immediately after the embargo was imposed on the DP business. These submissions are being made only to reiterate that, consequential penalties, by virtue of its inability to procure new customers have already been suffered by the broking business.*
- (vi) *Owing to the adverse orders by SEBI and pending proceedings, many stock broking and depository customers of KSBL, including institutional investors and high net worth investors, large corporate houses,etc., stopped transacting with KSBL. In addition to the same, owing to the embargo on opening of the demat accounts, which is a pre requisite for opening a broking account, KSBL was unable to procure new stock broking clients. As a result, the market share of KSBL took a nose dive, both in Cash segment and F&O segment. In terms of opportunities of revenue, the ban of those 19 months would have probably resulted in losing an opportunity to acquire around 150,000 customers, and, considering a yearly loss of revenue from these customers at a moderate Rs.50 crore, the loss in the broking business due to the embargo imposed on the DP business works out to a whopping Rs.500 crore over the last 10 years. It is submitted that SEBI should take this into account, while assessing or embarking on levying a further penalty on the broking business.*
- (vii) *It is a fact of pertinent importance that there has been a huge loss of market share. During a period when the equity cult was picking up, and where brokers were adding new customers and providing solutions, Kary had to face the ignominy of more than 1,00,000 existing customers, closing both their broking and their DP service accounts, during the subsequent 2/3 years. The more significant fact is that institutional investors for almost three years, large corporate houses, and a number of prestigious HNI individuals, some of whom are icons of business and industry, stopped transacting with Kary, because of the severe strictures passed, and because of the fact that there was a looming uncertainty over the future of Kary. It is submitted that SEBI should appreciate that it was almost a decade long effort for us to put together such institutional investors, HNIs, and corporate houses as our clients. It is also submitted that in the financial services industry, one activity feeds from the other. It is pertinent to note that this segment of investors, are also the investors who make investments in mutual funds, structured products, PMS, etc., all of which were impaired due to SEBI's punishment. It is submitted that the broking business, which forms the crux and the edifice of the structure, on which the entire group has been built, has suffered adequately already.*
- (viii) *Kary has been one among the few domestic/ non foreign brokers having a full-fledged license to operate as brokers in the U.S. It had been able to build and establish a name and a brand for itself over a period of time among investors, by providing information and research as a part in its services. Our services were also sought by FIIs, through our New York office, who used to solicit information and research from us on a regular basis. In the wake of the adverse judgement on its group entities*

and for different activities, and also in the wake of the fact that these charges were negative the broking business suffered as all this has resulted in these foreign investors curtailing, and thereafter stopping business with KSBL. KSBL had to reduce the number of research analysts and cut down on the business in the institutional segment due to the loss of business, and at this time when the research activity has once again commenced with a view to cover more than 300 midcaps, if an embargo as a ban on acquiring new customers is placed, all the new initiatives will suffer, causing tremendous loss.

- (ix) *It is submitted that on-line broking was introduced in the country during the year 2005-06 and there is no organisation in this country other than Karyy which was then in a better position to provide on-line services in view of the large investor base and its existence, country wide. With an excellent understanding of technology, and having understood all the nuances and the processes in the capital market, equipped with state-of-the-art IT infrastructure, KSBL was probably the only financial services intermediary in this country, and may be, even in the world, to have its own web-server, and also to possess a brand which has earned the confidence of various members of the public for its integrity, and its excellent service. It is further submitted that the ban on acquiring new depository accounts imposed on KSBL by SEBI was lifted on August 08, 2007. It was only subsequent to the lifting of the ban that KSBL was able to offer online broking services. As has already been indicated in the earlier paragraphs, on-line broking account cannot be opened without a demat account. Since August 2007, KSBL has opened around 4 lakh online / internet broking trading accounts. This however, is the residual list of investors, the cream of which had already gone to competition. Due to the restraint on KSBL's DP activity, KSBL- Broker was deprived of opening over 1.5 lakh online accounts.*
- (x) *The ban on opening new demat accounts for a period of 19 months had been tantamount to banning KSBL completely from its foray into on-line trading as also off-line broking, since it had become a practice of all customers using only one DP and a broker, due to which it could not even open a single on-line trading account. In other words, there has been, though not deliberate, a consequential penalty that has already been imposed on us by SEBI, as far as the broking operations of KSBL are concerned by virtue of the 19 months ban on opening new accounts as a Depository Participant. When the ban was lifted and KSBL commenced the process of opening on-line/internet broking accounts, it was among the first to provide the facility of giving the investor an option to trade online, or even for doing transactions off-line, when the investor did not have access to that facility.*
- (xi) *Further, many of the other businesses of Karyy group, including registry services, Mutual fund registry, Investment Banking activities, Distribution of IPOs, Mutual Funds etc. were also adversely affected owing to the negative publicity. The merchant banking arm of the Karyy group, Karyy Investor Services Ltd., was ranked No.2 in the year 2005-06, by Prime Database. It is humbly submitted that an investment banker must have the ability to place equity shares and get customers to subscribe for various IPOs. In view of the fact that KSBL was not in a position to acquire new customers by virtue of the fact that there was an embargo on its DP business, and also in view of the fact that the negative publicity was adverse, its ranking from No.2 in the year 2005-06 was down to No.15 in the year 2009-10. KSBL ranking as syndicate member and sub-syndicate member for IPO bidding, which was among the top 3, also came down to 13. It may be appreciated that this consequential loss had a prolonged impact on the entity.*
- (xii) *It is submitted that every large broking house in the country has an associate, or a subsidiary NBFC company. Karyy, with the same intent had therefore applied for an NBFC licence in December, 2005. Consequent to the adverse ruling of SEBI, the application for grant of registration as an NBFC made by Karyy in December, 2005, was returned in the month of August,*

2006, and, upon subsequently re-applying, Karvy received its registration as an NBFC for one of our subsidiary companies in April, 2009, i.e., after a lapse of four years. In these four years, the entire NBFC market was captured by the competition, and each of these NBFCs, are currently bigger by about 10 to 15 times than Karvy's size. Had Karvy been in a position to provide the required leverage and provided this facility to its customers, especially the broking customers, the revenue would have been much more. It is once again submitted that it was the broking business which had suffered a loss due to consequential impact by virtue of margin funding through NBFC not being made available.

The regulatory proceedings in the present matter have stretched for almost 10 years. The present peril and the Damocles sword of stoppage/restriction of the business has carried on for almost a decade. While, Karvy as a group has always co-operated and put in best efforts to facilitate the conclusion of these proceedings, there has always been a delay beyond the circumstances of Karvy due to which the proceedings have dragged on endlessly.

In addition to the loss of income, as illustrated above, the cost of running the business operations, including cost of retaining people and attracting fresh talent for the group also increased substantially during this period. The mere time taken of almost a decade of uncertainty of the future, and, a lack of visibility of their career, has taken a toll on the managerial personnel. We submit that despite the fact that a number of senior members of the organisation, especially those who are in key positions, and responsible for the operations of the company and the action taken at that point of time, having left the group, we have always cooperated, and we have always put in our best efforts to facilitate the provision of information and the conclusion of the proceedings. We submit that, regretfully, despite our endeavour to complete the proceedings as quickly as possible, these have dragged on endlessly. It would also be pertinent to point out that not only the basic information, but the information required for processing which will facilitate an investigation of SEBI into the IPO irregularities, was actually submitted by Karvy in the initial stages, to enable the regulator to take an informed decision, little knowing that these decisions would back-fire on us. In addition to the big challenges in retaining managerial personnel, especially in view of the uncertainties of the future, it is also becoming increasingly difficult for us to attract good talent, and, should we attract good talent, it will always be necessary for us to pay a compensation which is in excess of anywhere between 10% - 20% over the market to give confidence to the concerned new recruits, about the future of the organisation and the business.

According to the noticee, the following would be the impact of any punishment as proposed in the impugned order:

"It is pertinent to note that that KSBL presently opens more than 10000 broking accounts, per month. Given the improved market sentiments, there is significant opportunity of KSBL increasing its market share which was otherwise tepid on account of the reasons explained earlier including the restraint imposed on DP business. Even on a very conservative estimate, in the event the Impugned order is not set aside, the same would result in KSBL being not able to open almost 50,000 broking accounts and recurring annual loss of Rs. 44 crores till eternity (being the brokerage revenue that can emanate from these customers)."

In view of the submissions and the penalty already undergone by the noticee, the following request was placed by the noticee:

- (i) Charges in the captioned Notice be dropped and no penalty be imposed on KSBL.
- (ii) It would be pertinent for us to further submit that, should the punishment be levied as proposed in the impugned order once again, we would be losing at least 50,000 customers, because we presently acquired around 10,000 customers. This will result in a recurring annual loss of Rs.44 crore forever.
- (iii) If the charges that have been made against Karvy Stock Broking as a broker are looked at, it can be observed that the main charges are that of (a) Introduction of bank accounts for the key operators and fictitious names/benamis by KSBL (b) Bidding of IPO applications by KSBL and (c) Sale of shares (which were cornered by the key operators in the IPOs) through KSBL. As a syndicate member/sub-syndicate member, Karvy Stock Broking undertook the responsibility of bidding of applications. The purported introduction of bank accounts, collection of applications, and the bidding of the applications are all on account of the fact that KSBL was the syndicate member/sub-syndicate member, which forms part of the primary market activity. The role of a broker in the secondary market is only to buy and sell securities on behalf of various clients based on orders placed by them. There is no way that a dealer sitting in Dehradun, or Siliguri, or Simla, or Kanyakumari, or for that matter in Ahmedabad or Mumbai, should be penalised for an activity not within his purview. We also submit that should SEBI continue to hold the view that Karvy is guilty, the primary market activity undertaken by Karvy Stock Broking, who is responsible, at best, the penalty can be levied on the primary market segment by putting restrictions on the functioning as a syndicate member, which itself will be harsh, since we believe that this also should be restricted geographically, i.e., to Ahmedabad. It is submitted that if any penalty is proposed to be imposed the distinction between Primary Market and Secondary Market activities undertaken by KSBL be taken into account while determining punishment and penalty be restricted to activities undertaken by KSBL in the Primary Market as a Syndicate Member only. Since the allegations in the Notice are flowing from the activities undertaken by KSBL in the Primary Market as a Syndicate Member only. The allegations in the Notice have no nexus with the activities undertaken by KSBL in the Secondary market as a Stock Broker.”

I have considered the above submissions. As has been observed by SEBI in the Order against Karvy-DP, it is necessary to see the happenings in the matter related to IPO irregularities in a holistic perspective rather than in a fragmented way. As mentioned above, I am inclined to see the Karvy Group as closely knitted rather than truly independent entities. The business of one entity influences the business of other entities both in a positive and negative sense. I do not give much credence that an employee (i.e., Vyomesh Pandya) was not formally on rolls of one entity even as he acted purportedly on behalf of that entity. Therefore, I am inclined to consider the argument of Mr. C. Parthasarathy that the business of stock broking entity was adversely affected as the DP entity underwent 18 months ban on acquisition of new business, as clients normally like to have both broking account and demat account under the same roof. Therefore, the ban on DP entity is likely to have affected the business of the noticee in addition to the adverse effects of the 14 months restriction on proprietary business. The introduction of bank accounts and bidding of IPO applications are indeed not secondary market

activities. Keeping in view the fact that allegations emanate from IPO irregularities which is a primary market activity and not from any market manipulation (volume/price manipulation while trading in a stock exchange), I tend to appreciate the argument of the noticee.

15. On consideration of the above submissions made by the noticee as regards the 'penalty' including the following –

- (a) the above submissions made by the noticee and the penalty already undergone by it including the impact on its business and development of business by virtue of SEBI's earlier direction and also the impact on the stock broking business due to the restraints earlier imposed on the DP activities of the noticee,
- (b) the submission that the penalty should be with respect to the activities of the noticee in respect of its primary market business,
- (c) the findings made above in this Order,

I am of the view that this proceeding could be disposed of by the following Order.

16. In view of the foregoing, I, in exercise of the powers conferred upon me in terms of Section 19 of the Securities and Exchange Board of India Act, 1992 read with regulations 28 and 35 of the Securities and Exchange Board of India (Intermediaries) Regulations, 2008, hereby dispose of the proceedings by directing the noticee, Karvy Stock Broking Limited not to undertake new primary market assignment including acting as syndicate member or providing syndication services (procuring IPO applications and bidding in IPOs), directly or indirectly, in IPOs for a period of one year. In order to avoid inconvenience to any issuer/intermediary, it is clarified that this direction shall not hinder the activities for which the noticee was already engaged for undertaking primary market activities before the date of this Order.

PRASHANT SARAN
WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA

Date: June 15th, 2015

Place: Mumbai