BEFORE THE SECURITIES APPELLATE TRIBUNAL

MUMBAI

Appeal No.29/2002

In the matter of;

R.B. Khandelwal

(Director of R.B.K. Share Broking Ltd) Appellant

Vs.

Securities & Exchange Board of India Respondent

Appearance:

Shri T. N. Subramanian,

Advocate

Shri Prateek Seksaria,

Advocate

I/b Gagrat & Co., For Appellant

Shri J. Ranganayakulu

Jt. Legal Adviser, SEBI For Respondent

(Appeal arising out of the order dated 28.5.2002 made by the Chairman, Securities & Exchange Board of India)

ORDER

Yashodham Commercial Enterprises Ltd., (the company) came out with a rights issue of 9.9 lakhs equity shares of Rs.10/- each at a premium of Rs.5/- in the ratio of 4:1. The issue opened on January 25, 1996 and closed on February 24, 1996. It was reportedly fully subscribed. The company's financial results as revealed in the offer documents were not attractive enough to attract enthusiastic response from the investors. The company had not declared dividend in the five years preceding the rights issue. In the offer document it has been stated that there was no trading in the company's shares during April 1992 – August 1995. In September 1995, the high/low prices of the scrip was at Rs.99/- and Rs.55/- respectively. EPS was Rs.0.17 during the year 1994-95. The price movement was found abnormal and unrealistic. In that scenario, the Respondent. (SEBI.) decided to investigate. The preliminary investigation reportedly revealed that the price rise was artificial. By October 10, 1995 the company's share price had touched a high of Rs.160/- but plummeted to Rs.20/- by 30.1.96. The investigation concluded that the promoters and the persons in control of the company might have been involved in the price manipulation of the scrip with a view to inducing investors to subscribe to the company's rights

issue. It was found that Shri R. B. Khandelwal, a director of the Appellant was the Chairman of the company and he had dealt in the shares of the company during the period. SEBI further investigated the matter and prima facie found involvement of Shri R. B. Khandlwal in the price manipulation. In that context, on 3.1.2001 SEBI appointed an enquiry officer "to enquire into the affairs of Shri R. B. Khandelwal, Member BSE, in the dealings" in the company's scrip and possible violations of the Act, Regulations etc. The enquiry officer submitted his report on 30.10.2001 inter alia holding that Shri Khandelwal had failed to exercise due skill, care and diligence in the conduct of his business as broker. He recommended suspension of the certificate of registration granted to Shri Khandelwal for a period of 3 months. A copy of the enquiry report was forwarded to Shri Khandelwal asking him to show cause as to why the penalty recommended by the enquiry officer should not be imposed on him. Shri Khandelwal responded to the notice. SEBI's Chairman adjudicated the show cause notice. He came to the conclusion that Shri Khandelwal had failed to observe due diligence and exercise care as expected of a registered intermediary and found him guilty of violating clause A(2) of the Code of Conduct prescribed in the Securities and Exchange Board of India (Stock Brokers and Sub Brokers) Regulations, 1992 (the 1992 Regulations). In that context he ordered that "the certificate of registration of RBK Share Broking Ltd., Member, The Stock Exchange, Mumbai, be suspended for a period of one month" with effect from June 10, 2002. The order is dated 28.5. 2002.

The Appellant claiming to be aggrieved by the Respondent's order has filed the present appeal praying for its revocation. The Appellant had also prayed for interim order staying the operation of the impugned order pending disposal of the appeal. The prayer for interim order was granted, after hearing the parties.

Shri T. N. Subramanian, learned counsel appearing for the Appellant referred to the Respondent's order dated 3.1.2001 for holding enquiry into the "affairs of R. B. Khandelwal, Member, BSE in the dealings in the scrip of M/s. Yasodham Commercial Enterprises and possible violations of the provisions of following regulations by the said member:

a. Securities and Exchange Board of India Act, 1992.

b. Memorandum and Articles of Association, Regulations and Bye laws of (the) BSE

c. Securities and Exchange Board of India (Stock Brokers and Sub Brokers) Rules and Regulations, 1992

d. SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulation, 1995"

Shri Subramanian submitted that the order refers to the "contravention aforesaid" but no contravention has been stated in the order. He submitted that an order vaguely stating "possible violation of the provisions" of the Act and certain Regulations can not be considered as a proper order for holding enquiry against Shri Khandelwal. He submitted that the order does not refer to the specific provisions of the law stated to have been violated and it does not even mention the specific period of dealings in the scrip of the company to be brought under enquiry, that since the proceeding being a quasi criminal proceeding resulting in imposition of penalty it is all the more necessary that the order for holding the enquiry is specific and not vague without leaving its scope to the discretion of the enquiry officer. He submitted that the said deficiency in the order is not a trivial one to be ignored.

Shri Subramanian submitted that SEBI had admitted the fact that Shri Khandelwal had given a trading terminal to Anand Securities, one of his reputed clients/sub brokers, that all the dealings in the scrip of the company were done by Anand Securities, that Shri Khandelwal had not purchased/sold or invested in the said scrip or offered any shares in the auction. Learned counsel submitted that SEBI had viewed that since Shri Khandelwal while signing the contract notes should have found out the motives of the client, and having not done so should bear responsibility

for the irregularities in the transactions undertaken by Anand Securities. He submitted that Shri Khandelwal had explained to the enquiry officer as to the circumstances of his dealings in the scrip during its suspension period, that he was not aware of the suspension of the scrip, as it was not disclosed by BSE in the BOLT during the period, that SEBI had justified the failure on the part of BSE to disclose the fact of suspension of the scrip for the reason that the computerisation in BSE on line was started only on 1.7.95 and these transactions in the scrip during the suspended period upto 11.9.95 occurred during the period when everyone was learning, including BSE. Shri Subramanian submitted that the fact is that suspension was not prominently disclosed and the sales of that suspended scrip was not rejected by BSE.

SEBI, in its report has admitted Shri Khandelwal's submission that there was some problem in the on line trading system at the exchange level since these trades were recognised and the deliveries were settled/auctioned, and that if the scrip was under suspension, then these trades should have not been accepted in the first place nor settled. SEBI found this explanation acceptable as this related to the initial stages of on line trading in BSE. Learned counsel submitted that thus it is clear that the Respondent itself has admitted that everybody including BSE was learning and in that context any omissions or commissions taken place during that period should not have been magnified. He referred to the Respondent's observation in the enquiry report that "I find the member did not notice the motive of their client to manipulate the scrip of YCEL.The member could have come to know about this for reasons mentioned above. By not doing so and by allowing the client to operate, the member did not have any control on the operation of their terminal by the client. I hold that the member did not exercise due skill care and diligence in the conduct of business through Anand Securities" Shri Subramanian submitted that the said observation of the enquiry officer itself indicates that the charge of manipulation of the market by Shri R. B. Khandelwal is untenable as the Respondent himself has admitted that "Shri R. B. Khandelwal did not notice the motive of their client to manipulate the scrip of YCEL". He submitted that when the person was not aware of the motive of his client, he can not be held as a party to the acts of manipulation and proceeded against.

Shri Subramanian submitted that nowhere in the enquiry report, it has been stated that the Appellant was a party to the price manipulation. He stated the charge is that Shri Khandelwal did not find out the motive of Anand Securities. Shri Subramanian submitted that since Shri Khandelwal was not a party to the deal, he had no means to find out the motive of the person dealing with him. He submitted that only 0.33% of the total trading of Anand Securities was transacted with Shri Khandelwal. He referred to the total turn over figures and submitted that Anand Securities' share therein was trivial and it was not possible for a broker dealing in huge transactions to minutely scrutinise the details like registered office address etc. of the parties dealing with him and match the same with the company's address and see whether these were common. . He submitted that the registered address of the company and the parties did not indicate that they were sharing the same premises and they were associated with the company. In this context he referred to the address of the three entities and pointed out the difference as under:

Yashodham Comm.Enter. Ltd.	**Date upto 16/10/1995**	**Date from 16/10/95**
	7th, Khetwadi, 25th Khambatta Lane, Bombay 400 004.	16 C, 28, B.S. Marg, 3rd Floor, Fort, Bombay 400 023.
Mangal Bhawan Holding Pvt.Ltd.	**Date Upto 1/10/95**	**Date from 2/10/95**
	302, Gaurav Apartments, Gokuldam, Filmcity Road, Goregaon (E) Bombay 400 63	G-26, Gokuldam Shopping Centre, Gokuldam, Goregaon (E) Bombay 400 063
Anand Securities	**Date upto 16/10/95**	**Date from 16/10/95**
	16A, 28, B.S. Marg 3rd Floor, Fort, Bombay 400 023	16A, 28, B.S. Marg, 3rd Floor, Fort, Bombay 400 023

He submitted that from the details it could be seen that there is no "common address" as mentioned by the enquiry officer. The enquiry officer in his report had stated that proper care should have been taken while signing the contract notes and had Shri Khandelwal taken such care he would have noticed the association of Anand Securities with the company. There was no indication of common address of the entities giving any clue and hence there has been no negligence on the part of Shri Khandelwal, as alleged. He submitted that it is impossible for a borker in the normal course while signing contract notes to find out the motive of his clients in dealing in one of the scrips and that inability of the broker in uncovering the intentions of a client can not amount to any failure to exercise due skill, care and diligence in the conduct of his business, that there was nothing even to suggest that nature of the transactions of Anand Securities was not normal. Learned counsel submitted that it was impossible for any human being at that point of time to discover that there was an attempt on the part of the said Anand Securities to manipulate the market.

Learned counsel submitted that the Respondent has imposed the penalty of suspension on him stating that he has not exercised "due skill care and diligence" but the order has failed to establish the charge. He stated that failure to verify the address of a client by itself can not be considered as a matter warranting the severe penalty of suspension of registration resulting in deprivation of the business. He submitted that by the Respondent's own version Anand Securities is an abetter, but despite the same they were served a show cause notice only on 28.6.2002 obviously on knowing the challenge made by the Appellant in its appeal memorandum filed on 5.6.2002, that the show cause notice was issued only to

show that the Respondent has also proceeded against the said firm. Learned counsel submitted that if Anand Securities had manipulated the market, the proceedings should have been initiated against them in the first instance and not against Shri Khandelwal

Shri Subramanian submitted that the company's public issue was opened on January 25, 1996 and closed on February 24, 1996, that BSE and the Respondent were well aware of the price movement and volume movement in the scrip in the preceding months, and still the offer documents were approved by the Respondent, that after 5 years the Respondent started investigations. He submitted that the Respondent has now contended that the company's performance was poor, little realising that as early as on 16.11.1995 the Respondent had given permission to the company for the right issue at a premium of Rs.5/- per share. He also pointed out that the show cause notice has been issued only to Shri R. B. Khandelwal and not to the company. Shri Subramanian stated that Shri Khandelwal in his reply to the show

cause notice had clarified that he had not conducted trades personally either in his individual capacity or as a broker, that he had never recommended any of his clients, associates or friends to buy or sell shares of the company, that the trade referred to in the notice were effected by Aanand Securities who was his client and sub broker and at that time BOLT system was also provided to the said Anand Securities in Shri R. B. Khandelwal's office premises with the knowledge of BSE.

Shri Subramanian submitted that the findings recorded by the enquiry officer are based on mere conjectures and surmises, that the Respondent has viewed that Shri Khandelwal as the chairman of the company was in the know of things that he can not be unaware of the connection of the said Anand Securities with the company. He submitted that the Respondent has failed to establish any such knowledge or association of Shri Khandelwal with reliable material to support, little recognising the fact that he was only a non executive chairman.

Learned counsel submitted that the alleged failure relates to a period when the Appellant company was not even in existence. The Appellant company was incorporated on 12.4.1996 as a public limited company. The Appellant was given registration (bearing No. INB 010986236) by SEBI vide certificate dated 31.12.1997. He submitted that Shri Khandelwal was holding a separate registration as a stock broker bearing registration No.INB010022212 issued to him by the Respondent on 26.11.1992. He was carrying on the business of stock broker in his individual capacity. He ceased to be a member with effect from 30.12.1997. Shri Subramanian submitted that the Respondent initiated investigations and enquiry against Shri Khandelwal and Shri. Khandelwal appeared and presented his case before the Respondent. He submitted that the Appellant was not subjected to any enquiry. Despite so, the impugned order is directed to the Appellant. He submitted that the Respondent has chosen the Appellant to be punished after holding an enquiry into the conduct of Shri. Khandelwal who at the relevant point of time was not a director or even a share holder of the Appellant and for that matter the Appellant was not even in existence at that time, that it is not that the Respondent was unaware of this position, as the Appellant vide its letter dated 23.10.98 had brought to the notice of the Respondent that Shri Khandelwal and the Appellant are not one and the same entity. In this context Shri Subramanian cited the portion from the letter that "With reference to your letter dated 15.10.98 to the above mentioned scrip we would like to state that our firm RBK Share Broking Ltd., came into existence on 9th February, 1998. In the letter you have advised to give all the copies of all the Bank Accounts maintained by our firm for the period from 1st September 1995 to 30th July, 1996. Please clarify about your requirements as our firm was non existent and only proprietorship firm in the individual name R.B. Khandelwal was exist. Whether Bank details of all the clients or the account statement or the Bank details of R.B. Khandelwal is required by you so that we can submit the document as per your requirement for investigation in Yashodham Commercial Enterprises Ltd.," According to him the Respondent did not respond to this letter.

With reference to the observation made by the enquiry officer that Shri Khandelwal should have verified the transactions done by Anand Securities in the shares of the company, Shri subramanian referred to the transactions of Anand Securities and submitted that out of the total trade transactions of 1843 effected by Anand Securities, only 86 trades related to the company's shares, that in terms of value, the total value of the shares was Rs.14.89 crores of which the value of the company's share was just Rs.33 lakhs. He referred to the break up value of total purchase and sales of the company's shares (of Rs.3300000/-) and stated that out of the said total, purchase component was 18500 shares of the value of Rs.16,90,950 and sales component was 15500 shares of the value of Rs.15,93,300. The net quantity purchased was 3000 shares for a value of Rs.97650/-. He further stated that in sett. No.14, 1400 shares of the company got auctioned in which Anand Securities incurred a loss of Rs.50575/- hence adding this loss of Rs.50575/- the total purchase value of 3000 shares works out to Rs.148225/-, that the client never participated in any auction at the Appellant's end.

Shri Subramanian submitted that as the company's shares transacted by Anand Securities were only minuscule compared with the total transactions effected by the said party and as such there was no reason for Shri Khandelwal to believe that there was any manipulation or irregularity in the trading of the scrip of the company by Anand Securities. He submitted that if the transactions in the shares of a company are going beyond particular percentage it would have come to the notice of the broker but in the instant case the total transactions in the shares of the company was **0.33%** of the total volume of Shri. Khandelwal and 4.66% of the total volume of Anand Securities during the period in question and therefore it was not possible to put any surveillance on a day to day basis.

It was submitted that Anand Securities was Shri Khandelwal's client for couple of years, that they had fulfilled their commitment and never defaulted, that they were one of his reputed clients, hence when they were provided the BOLT terminal there was no cause of concern towards their responsibilities and commitment, that all checks and controls were supposedly built in the system itself by BSE , that all the trades have taken place as per the proper checks & measures terminals in fact have inbuilt security features, the system itself takes care of everything with care & due diligence. Shri Subramanian submitted that all margins were kept towards Anand Securities, that Shri Khandelwal had taken due skill care & diligence in conduct of business of Anand Securities that he had abided by all BSE Rules and Regulations and there is nothing to show any failure on his part in this regard.

Shri Subramanian explained the meaning of the expressions diligence, care, skill with the aid of Law Lexicon and submitted that by any standard, in the light of the given set of facts and concept as is understood, the Respondent's finding that Shri Khandelwal failed to exercise due diligence, skill and care is untenable.

Shri Subramanian submitted that the order imposing penalty cannot be sustained as the Appellant was not given even an opportunity to explain its stand, that the show cause notice issued to Shri Khandelwal and his reply thereto in his individual capacity can not be treated as the Appellant's reply. . He further submitted that the Respondent can not go beyond what the enquiry officer said, that if any variation there to, which is adverse to the noticee is to be effected, it can not be done without giving the person concerned an opportunity to put forth his case, and as such for any reason if it was felt that the Appellant should be brought in the purview of the enquiry, it was incumbent on the part of the Respondent to give it an opportunity to show cause. He submitted that the Respondent has ignored the Hon'ble Supreme Court's decision "to act justily and fairly and not artbitrarily or capriciously" as laid in A. K. Kraipak V. Union of India (AIR 1970 SC 150)

Shri Subramanian stated that the order is not a reasoned one and it is based

on conjectures and surmises, that the Chairman of the Respondent has simply adjudicated the erroneous conclusions drawn by the enquiry officer.

With reference to the penalty of suspension imposed by the Respondent, Shri Subramanian cited the following observations by the Hon'ble Supreme Court in Union of India v. H, C. Goel (AIR 1964 SC 364) that:

> "Though we fully appreciate the anxiety of the Appellant to root out corruption from public service, we cannot ignore the fact that in carrying out the said purpose mere suspicion should not be allowed to take the place of proof even in domestic enquiries . It may be that the technical rules which govern criminal trial in court may not necessarily apply to disciplinary proceedings, but nevertheless, the principle that in punishing the guilty scrupulous care must be taken to see that the innocent are not punished, applies as much to regular criminal trials as to disciplinary proceedings"

In this context he also referred to the observation made by this Tribunal in M. J. Patel V. SEBI ((2002) 38 SCL 889) and stated that the Respondent has not dealt with the defense put up by the noticee and the order has been passed without application of mind.

Shri Subramanian in support of his contention that no penalty is warranted in the case also cited Hindustan Steel Ltd., V. State of Orissa (AIR 1970 SC 253) that :

> "An order imposing penalty for failure to carry out a statutory obligation is the result of a quasi criminal proceeding and penalty will not ordinarily be imposed unless the party obliged either acted, deliberately in defiance of law or was guilty of conduct contumacious or dishonest, or acted in conscious

disregard of its obligation. Penalty will not also be imposed merely because it is lawful to do so. Whether penalty should be imposed for failure to perform a statutory obligation is a matter of discretion of the authority to be exercised judicially and on a consideration of all the relevant circumstances.

Even if a minimum penalty is prescribed, the authority competent to impose the penalty will be justified in refusing to impose penalty, when there is a technical or venial breach of the provisions of the Act or where the breach follows from a bonafide belief that the offender is not liable to act in the manner prescribed by the Statute."

Learned counsel submitted that only because of the directorship of Shri Khandelwal in the Appellant or for that reason he holds shares in the Appellant, the

Appellant cannot be penalised for the offence allegedly stated to have been commited by Shri Khandelwal.

Shri Ranganayakulu, learned Representative of the Respondent submitted that clearing of the offer document relating to the rights issue of the company by the Respondent does not mean that the Appellant can not be proceeded against for violation of the regulations. He submitted that the company's offer document was cleared and simultaneously investigation into the price manipulation in the shares of the company was ordered. He stated that stopping of the company's public issue, at that point of time, merely on suspicion without adequate information on hand, was considered an extreme measure, that while clearing the offer document the company was directed to disclose an additional risk factor in the offer document and accordingly it was disclosed in the offer document that "Although shares of the company are listed at Bombay and Calcutta Stock Exchanges, there was no trading during the years 1992-93, 1993-94 and 1994-95. The regular trading has started only in September, 1995. Quotations of the period after 1995 are based on very thin trading on the Stock Exchange and may not reflect the intrinsic value of the shares". Shri Ranganayakulu submitted that with this disclosure, it was left to the investors to decide as to whether the offer was worth responding.

With reference to the relationship of Shri Khandealwal with Anand Securities, he submitted that the said entity was the Appellant's client is evidenced

from the acknowledgement receipts of contract notes issued on 14.8.95, 17-8-95, 26.8.95 and 27.8.95 wherein Anand Securities has been shown as "client". He further submitted that the role of the said Anand Securities in the manipulation of the company's shares remains undisputed that Shri Khandelwal, by virtue of his association with the company and the concerned parties can not claim that he was unaware of the said firms association with the company. According to him Prakash

Gaggar was one of the promoters and the Executive Director of the company, that he was also the director of Mangal Bhavan Holding P. Ltd., that the said Mangal Bhavan Holding P. Ltd. was the proprieitor of Anand Securities at the relevant point of time and the And Securities and the company shared the same premises. Anand Security being a client of Shri Khandealwal and he having provided a terminal to them, it was his duty to ensure that his client did not indulge in manipulations, that the broker providing terminal to his client to transact business is accountable to the client's conduct. Learned Representative in this context referred to the relevant transactions mentioned in the enquiry report and stated that in the light of the same the Appellant cannot absolve itself from its obligations. He submitted that it is for the first time that the Appellant has claimed that Anand Securities was its sub broker from April 1995. He submitted that the transactions involved are of the same period, and therefore, the Appellant's version that Anand Securities was a stranger or had just started their dealing with the Appellant in the relevant period are baseless. According to the learned Representative, Anand Securities was not a sub broker of the Appellant, but they were its clients, it had done trade on behalf of Anand Securities as its sole client, that at no point of time during the course of investigation, the Appellant had stated that Anand was its sub broker. Shri Ranganayakulu submitted that since Anand Securities was not a sub broker but a client of the Appellant, the question of rules and regulations applicable to giving separate terminal to sub broker does not arise in the instant case.

Learned Representative further submitted that what is more relevant is the concentration of the client in the scrip of a company with which the client/broker is connected. Shri Khandelwal had not received the company's shares for delivery from Anand Securities for sales effected on their account in the very first settlement itself. i.e. settlement No.14, as it is observed that the buying member had received the shares in auction at a later date, that this again is a signal that should have alerted Shri Khandelwal and put him on guard about his client's dealings in the scrip. The

scrip was not traded for a period of three and half years from April 1992 to August 1995 i.e. prior to the rights issue, that during the said three and half years the scrip was in fact under suspension from February 1994 to September 10, 1995, that when the suspension was revoked by BSE on September 11, 1995 the trading opened at Rs.85/- and the next day the company submitted an application to BSE seeking permission to come out with a rights issue. The scrip price rose to a high of Rs.160/- by October 10, 1995 without any apparent reason of financial performance etc., that BSE thereafter shifted the scrip to spot delivery basis from 01.11.1995 and by January 30, 1996 the price dropped to Rs.20/-. He submitted that the price fluctuation in the scrip affected the investors.

Shri Ranganayakulu submitted that before accepting Chairmanship of the company, Shri Khandelwal must have enquired into the background and full facts of the company, that he can not be unaware of the fact that the company's shares were not traded / were under suspension for a very long time and that Anand Securities was connected/associated with the company. Shri Ranganayakulu refuted the Appellant's version that the enquiry officer and the Chairman of the Respondent had failed to disclose the responsibilities which the Appellant had not fulfilled/discharged, to hold the Appellant guilty of violating Clause A (2) of the Code. He submitted that the finding of the enquiry officer was very clear which, inter alia, stated that Shri Khandelwal did not notice the motive of the client to manipulate the scrip of the company that he could have come to know about this for the reasons mentioned in the enquiry report and that he allowed the client to carry on the activities unrestrained, that the Appellant provided the trading terminal to the client without exercising any control over the operation of the terminal by the client.

Learned Representative submitted that since the broker is liable for all the transactions put through his terminals, it is in his own interest to put in place proper systems, procedures and warning signals as would enable him to have oversight and control over transactions put through his terminals, that such systems and restrictions may depend upon the clients / sub-brokers networth etc. and it was for the Appellant to decide as part of the risk management to safeguard his position to ensure compliance with the code of conduct and if he has not done so, he cannot be absolved from the consequences.

. Shri Ranganayakulu, with reference to the Appellant's statement that the volume transacted was only 0.33% submitted that the volume of the trade transacted has to be taken with reference to the trading in the volume of the company's scrip and not with reference to the transaction by the Appellant as a whole, and that it is evident from the data furnished by the Appellant that it was not negligible as claimed.

Learned Representative submitted that neither the enquiry officer nor the Appellant has gone beyond the scope of the show cause notice and the Chairman's order to conduct enquiry is wide in scope and has given a general mandate to the enquiry officer. The scope and reach of the enquiry is decided by the show cause notice, that the notice issued in this regard clearly indicates the charges and the applicable legal provisions and the enquiry was confined to the ambit of the notice. He submitted that the allegation that the order has been passed without giving opportunity to the Appellant is baseless, as it is on record that the Appellant had participated in the enquiry proceedings.

Shri Ranganayakulu submitted that the enquiry officer having taken into consideration all aspects, viewed that the appellant did not exercise due skill, care and diligence, as required vide Clause A(2) of Code of Conduct prescribed in Schedule II of the Regulations, and the Chairman concurred with the above finding

of the enquiry officer and ordered suspension of the certificate of registration granted to the Appellant for a period of one month.

With reference to the imposition of penalty against the Appellant in the enquiry initiated against Shri Khandelwal, Shri Ranganayakulu submitted that the Appellant is a closely held company of Shri Khandelwal, that substantial number of shares in the company are held by Khandelwal family that Shri R. B. Khandelwal himself is a director in the company. According to him the Appellant is nothing but an alter ego of Shri Khandelwal. In this context he referred to the Respondent's letter dated 30.12.1997 addressed to the Executive Director of BSE wherein the Respondent had asked BSE, to inter alia obtain an undertaking from certain persons (including the Appellant) to whom registration certificate was issued as Member of the Exchange that "an undertaking to the effect that all the rights/obligations and liabilities of the transferor will be honoured by the transferee" He also referred to the undertaking given by the Appellant (duly signed by Shri Khandelwal as designated director) that "We hereby undertake that RBK Share Broking Ltd., will honour all the obligations and liabilities including Bad deliveries etc. of the M/s. Radhesyam B. Khandelwal clg. No.585 since the commencement of his business in the market."

Learned Representative referred to the decision of this Tribunal in SKDC Consultants V. SEBI {(2001) 30 SCL 208 }and stated that the ratio of the said decision is not applicable to the present case as the

Appellant company is virtually owned and controlled by Shri Khandelwal.

I have considered the rival contentions put forth by the parties and the material relied on by them. My views are as follows:

According to the Respondent's version, the company came out with a rights issue of 9.9 lakhs equity shares of Rs.10/- each at a premium of Rs.5/- in the ratio of

4:1 in January /February 1996. The company's paid up capital was only Rs.24.75 lakhs before the said rights issue. The company's financial position was not rosy. It had not declared dividend for the preceding 5 years. The earning per share in the year 1994-95 was Rs.0.17. There was no trading in the company's shares on BSE for about three and half years. The trading in the shares on BSE was suspended for the period February 94 till 10.9.95. The suspension was revoked on 11.9.1995. Immediately on revocation of the suspension there was sudden spurt in trading at very high prices. Settlement wise price/volume details for settlement 14-17 (BSE) of 1995-96 covering the period 11.9.95 to 13.11.1995 have been stated in the order itself. It is seen that closing price of the scrip had touched Rs.132.85 in Settlement No.16. In Settlement No.17, the share closed at Rs.98/- though the opening quote was Rs.140. The higher price of the company's scrip would have attracted the attention of the investors and its impact on the company's proposed rights issue is imaginable. In the light of the attendant factors it is clear that the price hike was artificial to woo investors to buy shares in the company's proposed rights issue.

According to the Respondent, Shri R. B. Khandelwal (proprietor – Radheshyam B. Khandelwal – Member, BSE) was the Chairman of the company and that he personally knew the promoters of the company and he had dealt in the shares of the company on behalf a single client namely Anand Securities who was associated with the company, that Shri Khandelwal had done the maximum number of deals as well as volumes and had put through trades at prices which could not be justified for a scrip which was not at all traded for about 3 years. It is noticed that these transactions relate to September--November, 1995 period. It is seen that the Respondent had granted a registration to Shri Khandelwal in the year 1992, to carry on the activities of stock broker. His registration No. was INB010022212. He was holding the said certificate of registration till 30.12.1997. On 30.12.1997 he surrendered the certificate of registration. It is clear from the order that the Respondent had concluded that Shri Khandelwal was involved in the alleged manipulations and a show cause notice was issued to him on 9.2.2001 asking him to explain as to why action should not be taken against him under the 1992 Regulations for the alleged participation in the market manipulation. He responded to the notice, by making written and oral submissions before the enquiry officer/Chairman. On a perusal of the show cause notice I find that the charges are against Shri Khandelwal and the enquiry was also directed against him only. It is noticed that the Appellant company was incorporated as a public limited company on 12.4.1996 with the main object of carrying on stock broking business. The company got a registration from the Respondent for the purpose on 31.12.1997. Its registration number is IN B 010986236. Shri Khandelwal is one of the directors of the Appellant. He holds about 46% of the shares in the Appellant. His family members also hold shares in the Appellant. It appears that the Appellant is virtually under the ownership and management of the Khandelwal family. The fact that it is a public limited company and therefore, it is separate and distinct from Shri Khandelwal has to be borne in mind. That is why the Respondent granted separate registration to the Appellant. The enquiry was directed against Shri Khandelwal only. There is nothing on record to show that any enquiry was directed against the Appellant. The fact that the Respondent also felt that the Appellant cannot be held responsible for the omissions and commissions of Shri Khandelwal is demonstrated by the Respondent's own decision to grant registration to the Appellant as a Depository Participant as is seen from the letter dated 27.2.2001 to the Appellant from Central Depository Services (India) Ltd. It has been stated in the said letter that "SEBI has informed us vide their letter No. SMDRP/CDSL/24631 dated February 26, 2001 that your application has been found eligible for grant of Certificate of Registration as Depository

Participant in terms of Regulation 20 of the Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996……." It is to be noted that the Respondent's decision to grant certificate of registration as Depository Participant is of February 26, 2001 i.e. after the issuance of the show cause notice to Shri Khandelwal. It is difficult to believe that the Respondent would have given such clearance to a person who is facing an enquiry relating to market manipulation in a public issue of shares. Any connection with market manipulation could have stood in the way of granting registration to the Appellant as a Depository Participant. It is seen that the Appellant had written a couple of letters to the Respondent relating to the ongoing enquiry against Shri Khandelwal regarding supply of information. The fact that the Respondent had not felt it necessary to bring the Appellant in the ambit of the enquiry is evident from the material on record. The Appellant vide its letter dated 23.10.1998, had in response to a letter of the Respondent dated 15.10.1998 i.e. even before the formal show cause notice was issued to Shri Khandelwal, stated that "We would like to state that our firm R.B.K Share Broking Limited came

into existence on 9th February 1998. In the letter you had advised to give all the copies of all bank accounts maintained by our firm for the period 1st September, 1995 to 30th July, 1996. Please clarify about your requirements as our firm was non-existance and only proprietorship firm in the individual name R. B. Khandelwal was exist. Whether bank details of all the clients or the account statement, or the bank details of R. B. Khandelwal is required by you so that we can submit the document as per your requirement for investigation in Yashodham Commercial Enterprises Ltd.,"

Obviously this letter was issued when the investigation was going on which preceded the enquiry. There is nothing on record to show that the Respondent ever responded to the letter and provided any clarification. After investigation enquiry was initiated. The enquiry went on, wherein Shri Khandelwal participated and defended his case. In this context it is to be noted that Shri Khandelwal who was put on notice for his involvement as the proprietor of the stock broking firm which he was running in his name and the transactions covered by the enquiry related to a period when the Appellant was not even in existence. It is also to be noted and understood that Shri Khandelwal and the Appellant are two separate legal entities. It is not the Respondent's case that Shri Khandelwal had indulged in market manipulation as a director of the Appellant. If at all the charge sustains it is attributable to Shri Khandelwal's individual "conduct" for which a public limited company cannot be held responsible. The fact that the Appellant is owned and controlled by Shri Khandelwal family does not make any difference, as the question here is not taking over liability or obligation arising out of the business of the erstwhile proprietory concern, by the Appellant by virtue of any agreement or undertaking but submitting to penalty for an offence, allegedly committed few years ago by a person, when the Appellant itself was not in existence . The Respondent holding the Appellant guilty of violation of a statutory provision stated to have committed by someone, at some time before the company was incorporated, is not legally tenable. The Appellant can not be substituted in the place of Shri Khandelwal and considered as the "offender"

The Tribunal had occasion to consider more or less a similar issue in SKDC Consultants Ltd., V. Shri P. Sri Sai Ram (2001) 30 SCL 208 : (2001) 41 CLA 72) SKDC was a sole proprietory concern of one Mrs. Padma Sreedharan and the said proprietory concern's business was transferred to SKDC Consultants Limited on 1.4.98. SKDC was carrying on activities of Registrar to public issue. The said propreitory concern failed to comply with certain statutory requirements while acting as Registrar to an issue, some time in the year 1995. Respondent adjudicated the matter and imposed monetary penalty for the said failure on the said company. Aggrieved by the said order the said company filed an appeal in the Tribunal. The Tribunal while allowing the appeal observed

> "the Appellant came into existence on its incorporation on 18.02.1998 and
>
> thereafter with effect from 01.04.1998 it took over the business of SKDC as a going concern with all its assets and liabilities. It is clear from the adjudication order that the alleged violations relating to public issue of shares relate to November/December, 1995 and activities of Share Transfer Agent carried out prior to 02.02.1998, i.e to a period prior to the incorporation of the Appellant .

In this context it is to be noted that the Appellant is a distinct legal

> personality from SKDC. The fact that the Appellant had taken over the business of the said SKDC or that Mrs. Padma Sreedharan, the sole proprietor of the said SKDC, is one of the 7 subscribers to the Memorandum of Association and that she is one of the first directors out of the 4 directors of the Appellant is not sufficient to hold that the said SKDC and the Appellant are one and the same entity for all purposes. It may not be forgotten that the Appellant is a public limited company and not even a private company owned by the said Mrs.Padma Sreedharan. The agreement between the Appellant and SKDC provides only for transferring the ongoing business with all the assets and liabilities of SKDC to the Appellant. The Adjudicating Officer had concluded that SKDC had failed to comply with the requirements of rule 4(1)(b) well before the Appellant was brought into existence. In terms of section 15B, the penalty provided therein is to visit the person who had failed to comply with requirement of entering into agreement with his client. In this context it is to be remembered that the Supreme Court in Hindustan Steels Ltd., Vs. State of Orissa (AIR 1970 SC 253) had observed that " An order imposing penalty for failure to carry out a statutory obligation is the result of a quasi criminal proceeding". It is not possible to assign the " failure" in complying with a statutory requirement to some one else who was not responsible for the same and make him suffer the penalty attendant to such failure. If there is any liability to pay penalty by way of punishment, that cannot be transferred to a successor as it remains the liability of the person who committed the offence. The liability is personal to the offender. Therefore, the adjudication order holding the Appellant in

default for not complying with provisions of rule 4 (1)(b) and imposing monetary penalty on it for the said default cannot be sustained. The fact that the assets and liabilities of SKDC have been taken over by the Appellant does

not mean that it is responsible for the offence committed by SKDC and liable to suffer the penal consequences.

As the adjudication order is misdirected to the Appellant, it cannot be sustained."

I do not find any reason to take a different view in this case. In fact in the SKDC case atleast a show cause notice was issued to the company and subjected to enquiry and thereby it was given sufficient opportunity to put forward its case. In the instant case, the Appellant was not even given notice or subjected to investigation/enquiry, that only because the Appellant is owned and controlled by Khandelwal family, for an offence committed by Shri Khandelwal in his individual capacity that too at a time when the Appellant was not even in existence, the Appellant is held liable and made to suffer the penal consequences. The argument that the Appellant has taken over all the obligations and liabilities of Shri Khandelwal's proprietory firm, can not be stretched to hold the Appellant guilty of the offence committed by the said Khandelwal and liable to suffer punishment for the offence which it has not committed.

Since the order is misdirected to the Appellant it can not be sustained. For the said reason I do not consider it necessary to examine the other arguments advanced by the Appellant's counsel as the scope of the present appeal is with reference to the reach of the impugned order on the Appellant and not on Shri Khandelwal. .

For the reasons stated above, the appeal is allowed and the impugned order is set aside.

(C.ACHUTHAN) PRESIDING OFFICER

Place: Mumbai

Date: September 25, 2002.