BEFORE THE SECURITIES APPELLATE TRIBUNAL MUMBAI

Appeal No. 131 of 2012

Date of decision: 16.7.2012

Piyush P. Avlani
68/5, Govind Sadan,
C-25 Road, Sion (West),
Mumbai – 400 022. …Appellant

Versus

Securities and Exchange Board of India
SEBI Bhavan, Plot No. C-4A, G Block,
Bandra Kurla Complex, Bandra (East),
Mumbai - 400 051. …Respondent

Mr. P.N. Modi, Advocate with Mr. Prashant Ingle and Mr. Neville Lashkari, Advocates for Appellant.

Mr. Shiraz Rustomjee, Senior Advocate with Mr. Mobin Shaikh, Advocate for the Respondent.

CORAM : P. K. Malhotra, Member & Presiding Officer (*Offg*.)
S.S.N. Moorthy, Member

Per : S.S.N. Moorthy

This order will dispose of two appeals namely Appeal no.131 and 133 of 2012. Counsel for the parties agree that facts of the case and issues raised in the appeals are identical in nature and the appeals can be decided on the basis of facts contained in Appeal no.131 of 2012.

2. The appellant is an individual who trades regularly in the securities market. The present appeal is filed against an order passed by the whole time member of the Securities and Exchange Board of India (for short the Board) acting under section 11 read with section 19 of the Securities and Exchange Board of India Act, 1992 (referred to hereinafter as the Act) by which the appellant was restrained from accessing the securities market prohibiting him from buying, selling or otherwise dealing in securities directly or indirectly for a period of 2 years. The impugned direction under section 11 of the Act was issued since the appellant was found to have violated regulations 3 and 4 of the Securities and

Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 (FUTP Regulations).

3. The facts of the case, in brief, are the following. In March, 2009, M/s. Mahesh Kothari Share and Stock Brokers P. Ltd. (M.K.) approached the appellant seeking a loan against the shares of Alka Securities Ltd. (the company). The appellant agreed to lend a sum of ` 72,37,000 to M.K. and in turn M.K. agreed to provide security of 4,00,000 shares of the company. M.K. transferred the said 4,00,000 shares of the company to the demat account of the appellant on March 28, 2009 and the appellant gave the loan amount to M.K. on March 30, 2009. The appellant kept the shares of the company intact in his demat account without any transaction whatsoever in the said shares. The appellant received the said shares of the company in off market transaction and he did not deal in the shares of the company after March 28, 2009 in any manner. The Board observed a spurt in the volumes of the scrip of the company during the period November 2008 to March 2009. In September 2008 the closing price of the scrip was ` 32.45 while it reached a high of ` 35.05 in the same month and experienced fluctuations thereafter. After a stock split it reached ` 32 in May 2009. The Board also received surveillance alerts regarding the shares of the company. It was noticed that the promoters of the company transferred large quantities of the scrip in off market transactions and subsequently traded the same shares on the stock exchange. On account of the unusual market movement of a large chunk of the shares of the company the Board passed an ex-parte order on July 28, 2009. By way of this ad-interim ex-parte order the appellant was prohibited from buying, selling or dealing in the securities of the company till further directions. The ad-interim ex-parte order was passed on the observation of the Board that the promoters of the company along with several other entities had indulged in manipulative trades with the intention of creating artificial volumes so as to give a misleading impression about the liquidity of the scrip. The appellant, in its reply, explained that he was not engaged in the dealing of the shares of the company in any manner and his role was confined only to extending loan facility to MK. On October 30, 2009 the Board passed an interim order confirming the directions issued in ex-parte ad-interim order. The appellant has been considered a party to the manipulative actions of the promoters of the company since he was found to have been involved in the transfer of the shares of the company with MK. The appellant filed a detailed reply denying all the allegations in the

confirmatory order. Subsequently, on December 27, 2010 a show cause notice was issued to several entities including the appellant holding them guilty of acting in connivance with the promoters of the company in circular trades aimed at creation of artificial volumes and enhancing the image of the scrip in the public eye. The appellant filed a comprehensive reply to the show cause notice which was followed by a personal hearing. The appellant denied all the allegations. However, the whole time member of the Board, after considering the explanations offered by the appellant, passed a final order in respect of several entities, the appellant being one among them, confirming the stand already taken in the earlier orders. The appellant challenges the directions of the whole time member in the present appeal.

4. The facts of the case and sequence of the events are identical in the case of Ketan Joshi but for the difference that he had extended a loan of ` 1,50,29,000 on the security of 8,00,000 shares of the company.

5. Shri P.N. Modi, learned counsel for the appellant stoutly opposed the directions issued by the whole time member. According to him, the role of the appellant in the whole chain of events is confined to only providing a loan of ` 72,37,000 on the security of 4,00,000 shares of the company. According to him, the appellant is not connected to the promoters of the company and he did not trade directly or indirectly in the shares of the company provided to him as security and the shares are kept intact till date. The loan was granted on the basis of an agreement between the parties and the shares were transferred to his demat account so as to ensure the appellant's hold over the shares and to ensure security for the loan in the event of future default. It is admitted that the appellant came into possession of the shares on March 29, 2009 which is at the fag end of the investigation period and he did not possess the shares during a major part of the period under investigation. With a reference to the transactions in the shares of the company it is submitted by the appellant that even during the interregnum i.e. March 2009 to July 2009 (when the ex-parte ad-interim order was passed) the appellant did not trade in the shares of the company even though there was hectic trading in the shares during the said period. The appellant had no role in the circular/manipulative trades highlighted by the whole time member since he did not trade in the shares. It follows from the above, according to the appellant, that he has not contributed in any manner to the violations of the FUTP

Regulations. It is admitted that the appellant had taken possession of the shares in the nature of a security, pure and simple, and there was no pledge of the shares so as to invoke the provisions of Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996 (referred to hereinafter as the DP Regulations). It is contended that law does not prohibit any person from insisting on security of his choice and in the present case the appellant has adopted a simple and workable form of security shorn off all legal complexities. With reference to the charge leveled against the appellant it is argued that the whole time member has failed to establish the charge as against the appellant in as much as the role of the appellant in the alleged manipulation has not been established. It is also submitted that the appellant is engaged solely in the business of share trading and a ban of 2 years from the market would lead to disastrous consequences.

6. Shri Shiraz Rustomjee, learned senior counsel appearing for the Board defended the order of the whole time member observing that the role of the promoters and all the noticees considered in the impugned order along with the appellant should be considered holistically to appreciate the mischief in this case. With reference to the impugned order he submitted that the promoters and the impugned entities in the order resorted to off market transactions in a large quantity of shares of the company and then indulged in trading in the market in order to bring back the shares to the promoters with the intention to inflate the volumes and thereby hoodwink innocent investors. He would argue very strenuously that the appellant by virtue of the shares pledged with him, contributed to circular trade and so he has been charged with the violation of FUTP Regulations. The overall structure of the transaction has been made out in a manipulative manner and the movement of shares running to several crores establishes a well thought out game plan in which the appellant is seriously involved. According to him, the case of the appellant should not be viewed in isolation and identical replies given by the parties show the meeting of minds and manipulative intent. With reference to the appeal memorandum he submitted that the transaction in shares has been considered by the appellant to be a pledge without conforming to the legal formalities set out for a pledge and this is a glaring mistake on the part of the appellant. It was also observed by him that the loan document which is part of the records was not produced at the stage of personal hearing, but only afterwards. In short, he submitted that the role of the

appellant is vital in the chain of events when the background of the case and manipulation in shares are viewed in proper perspective.

7. We have considered the rival submissions. In the impugned order the appellant is held guilty of violating regulations 3 and 4 of the FUTP Regulations. For ease of reference, the above regulations are extracted below:

> "3. Prohibition of certain dealings in securities
>
> No person shall directly or indirectly-
>
> (a) buy, sell or otherwise deal in securities in a fraudulent manner;
>
> (b) use or employ, in connection with issue, purchase or sale of any security listed or proposed to be listed in a recognized stock exchange, any manipulative or deceptive device or contrivance in contravention of the provisions of the Act or the rules or the regulations made there under;
>
> (c) employ any device, scheme or artifice to defraud in connection with dealing in or issue of securities which are listed or proposed to be listed on a recognized stock exchange;
>
> (d) engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person in connection with any dealing in or issue of securities which are listed or proposed to be listed on a recognized stock exchange in contravention of the provisions of the Act or the rules and the regulations made there under.
>
> 4. Prohibition of manipulative, fraudulent and unfair trade practices
>
> (1) Without prejudice to the provisions of regulation 3, no person shall indulge in a fraudulent or an unfair trade practice in securities.
>
> (2) Dealing in securities shall be deemed to be a fraudulent or an unfair trade practice if it involves fraud and may include all or any of the following, namely:-
>
> (a) indulging in an act which creates false or misleading appearance of trading in the securities market;
> (b) dealing in a security not intended to effect transfer of beneficial ownership but intended to operate only as a device to inflate, depress or cause fluctuations in the price of such security for wrongful gain or avoidance of loss;
> (c) advancing or agreeing to advance any money to any person thereby inducing any other person to offer to buy any security in any issue only with the intention of securing the minimum subscription to such issue;
> (d) paying, offering or agreeing to pay or offer, directly or indirectly, to any person any money or money's worth for inducing such person for dealing in any security with the object of inflating, depressing, maintaining or causing fluctuation in the price of such security;
> (e) any act or omission amounting to manipulation of the price of a security;
> (f) to (r) ……."

8. It is necessary to examine the charge leveled against the appellant in the backdrop of the aforesaid Regulations. The whole time member made the following preliminary findings:

> "The trading activity by the promoter/company connected entities suggests circular trading activity with an intention of creating the volume so as to give the market a false impression about the liquidity of the scrip. The activities of the aforesaid entities are an attempt to attract unsuspecting investors to deal in the scrip. The related motive of maintaining trading price at artificial levels may arise from the fact that 74% of promoter shares were pledged against loans. The promoters and entities (1st level and 2nd level entities) connected to the promoters and company appear to have violated the provisions of Regulation 3 and 4 of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003."

9. "In the confirmatory order the whole time member observed thus:

> "the prima facie role of the entities in respect of their dealings in the shares of the company and the alleged violations committed by them were brought out in the ex-parte order. Though, Mr. Ketan H. Doshi and Mr. Piyush P. Avlani stated that they had not traded during the investigation period, they were found to have been involved in the transfer of the shares of the company with Mahesh Kothari Share and Stock Brokers Private Limited (an entity connected to the company) on March 28, 2009 i.e. during the relevant period."

10. In the impugned order the whole time member has reiterated the charge as under:-

> "Investigation, *inter-alia*, revealed that that ASL, in connivance with the promoters, 1st level, 2nd level and Additional Entities (the list of Promoter level entities, 1st level entities, 2nd level entities and Additional Entities are attached as Annexure A to this order), entered into transactions with a view to circulate the shares of ASL amongst themselves. It was therefore alleged that such acts were in violation of the provisions of Regulations 3(a), 3(b), 3(c), 3(d) and 4(1) & 4(2)(a), (b) and (g) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices) Regulations, 2003 (hereinafter referred to as 'PFUTP Regulations'). In addition the above, three (3) other entities, namely, JMDE Packaging & Realties Ltd , Alpha Graphic India Ltd and Takeshi Marketing Pvt. Ltd., were also alleged to have violated Regulation 4(2)(e) of the PFUTP Regulations."

11. The fact regarding provision of loan by the appellant on the strength of securities of the shares of the company remains undisputed. It is also not disputed that the appellant did not transfer the shares of the company in any manner after they came into his possession. So, admittedly, the role of the appellant is that of a mere financier. It is stated that the appellant is not connected with the promoters or other entities in the impugned order in any manner. The appellant extended the loan only at the end of March, 2009 i.e. at the fag end of the investigation period. In the replies filed by the appellant at various stages during the proceedings it has been stated in categorical terms that his role ended with the provision of loan to the promoters. He has no intention to trade in the shares nor does his conduct show any intention to participate in the alleged circular trades. It is true that the whole time member has made out a chart showing the movement of the shares during the period under consideration (Page 46 of the appeal paper and page 16 of the impugned order). However, the role of the appellant in the manipulative activity vis-à-vis the promoters and other

entities has not been established. The mere fact that a loan was extended by the appellant and the promoters of the company whose shares were kept as security with the appellant indulged in certain suspicious transactions may not involve the appellant in the web of mischief unless his active role in the process is brought out. The learned senior counsel for the Board drew our attention to the background of the case and insisted that the whole game plan and operation of the same should be viewed holistically. On the basis of the facts on record, we are unable to appreciate as to how the appellant can be linked with the manipulative game plan alleged by the whole time member. Unlike many of the entities involved in the transactions by way of trading in the shares, the appellant has kept aloof without even a single trade in the shares of the company. So we are unable to see any clear finding in the impugned order regarding the role of the appellant in the manipulative process which has been alleged against him.

12. The appellant has taken a consistent stand throughout the proceedings that the shares of the company were kept with him as securities for the loans provided by him. According to him, he wanted to have a higher level of security by transferring the shares in his name so that future litigation could be avoided. Accordingly, a loan agreement was duly entered into between the parties. In the reply filed by the appellant on August 11, 2009, the nature of the transaction has been spelt out by him in very clear terms:

> "I was approached by MK for finance against security of shares in around the 3rd week of March 2009. I was informed that owing to certain reasons, they had to urgently raise finance to meet certain commitments. They were ready to give security of marketable and freely transferable shares of their group listed company. We agreed on terms of the finance. Considering the facts involved and my judgment of the matter, I insisted that I should get absolute control over the security and I should not be made to resort to complicated and long drawn legal proceedings to recover my monies if the need so arose. Hence, I insisted that the shares be transferred in my name and I was ready though to give confirmation to them that I would transfer the shares back to them when they repaid my loan with interest. This was duly done."

13. The facts of the case show that the appellant has acted in accordance with his intention expressed hereinabove and there has been no attempt to transfer the shares in whatever manner.

14. The learned senior counsel appearing for the Board drew our attention to the statements made by the appellant on various occasions that the shares of the company were taken by him by way of pledge. According to him, pledge of property has got a special legal connotation in the Indian Contract Act and DP Regulations. It is stated by him that if law

lays down a certain manner of doing things it has to be done only in that manner and not in any other way. With reference to the various replies given by the appellant and the grounds taken in the appeal memorandum the learned senior counsel for the Board argued that the appellant has not complied with the requirements of a proper pledge and the conduct of the appellant was suspicious from the very beginning. It is true that the appellant has used the term 'pledge' in various parts of the reply furnished by him and also in the grounds of appeal. But we do not consider it necessary to analyse the nuances of pledge, bailment and other concepts in the present case since this is a case of providing security for loan, pure and simple. In the impugned order there is no material to establish that the appellant was engaged in fraudulent practices by resorting to pledge of the impugned shares and there by conniving with other entities in the scheme of things. In fact, there is reference to regulation 58 of the DP Regulations which deals with the manner of creating pledge or hypothecation of dematerialized shares. However, no charge has been made out on the basis of the default, if any, in this respect. In any case, we do not find it necessary to enter into an examination of the nature of security in this case. The facts of the case show that the appellant has insisted on a proper security to safeguard his interest. This was provided by MK. It is not necessary to go beyond this fact in the present case.

15. The learned senior counsel for the Board drew out attention to the loan agreement entered into between the appellant and MK and observed that it was filed only after the personal hearing in the case and non filing of the loan agreement during the proceedings of the case gives room for suspicion. We cannot appreciate the argument of the learned senior counsel for the Board in as much as the loan agreement is part of the record. It is true that it was filed after personal hearing was over. However, it was available to the whole time member before the finalization of the impugned order. He could have investigated into the matter if he felt so. This has not been done. In fact, no adverse inference has been drawn in the impugned order about the loan agreement. So nothing much turns on the late filing of the loan agreement.

16. We have already observed above that the appellant retained the shares with him and in the absence of any transfer of shares we cannot attribute any manipulative intent. The observation of the whole time member in the impugned order with regard to this aspect of the case is worthy of reference.

> "Further, certain noticees have argued that their holding in ASL shares remains virtually intact, and this indicates that the shares were not transferred but rather pledged to these entities. It is pertinent to note that the entire scheme of manipulation came to a standstill by the interim order in this matter, because of which several entities may not have been able to transfer the shares received by them to manipulate the scrip. Hence, this argument holds no merit."

It is to be noted that there was an interval between the receipt of shares by the appellant and the passing of the interim order by the whole time member. During the interval the shares were commanding good price in the market. Even then, the appellant did not part with the shares. So the consistent stand taken by the appellant regarding retention of the shares by way of security stands vindicated. The observation of the whole time member quoted above does not point to any specific instance of manipulation by the appellant.

17. We do not find it necessary to go into the case laws referred to by the parties since the facts of the case stand on their own right and the case laws cited by the parties may not in any way add to the strength of the case.

18. The conduct of the appellant established that he was not connected with the entities involved in the transactions and he has no role in the transfer of shares which is the foundation of the alleged manipulative transactions by the various entities in the case. In the absence of transfer of shares which were retained by the appellant no manipulative intent can be attributed to him. No connection or link with the entities involved in the impugned transactions has also been established. The appellant's basic activity of business is trading in the securities market. Debarment for a period two years is a very harsh punishment for a person of his kind. In the present case, no wrong doing attracting the provisions of FUTP Regulations has been established in the impugned order.

In view of the discussion above, we set aside the order of the whole time member and allow the appeal. No costs.

Sd/-
P.K. Malhotra
Member &
Presiding Officer (*Offg*.)

Sd/-
S.S.N. Moorthy
Member

16.7.2012
Prepared and compared by
RHN