BEFORE THE SECURITIES APPELLATE TRIBUNAL MUMBAI

Appeal No. 13 of 2013

Date of Decision : 19.06.2013

M/s. Ess Ess Intermediaries
Anand Saurashtra Society,
Opp. Devdeep Duplex,
Mahalaxmi, Paldi,
Ahmedabad- 380 007. …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. Deepak R. Shah, Advocate for the Appellant.

Mr. Prateek Seksaria, Advocate with Mr. Akhilesh Singh, Advocate for the Respondent.

CORAM : Jog Singh, Member & Presiding Officer *(Offg.)*

Per : Jog Singh

1. The Appellant, who is a sub-broker based in Ahmedabad (Gujarat), has preferred the present appeal against the Impugned Order dated December 14, 2012, hereinafter referred to as "Impugned Order", passed by the Securities and Exchange Board of India, hereinafter referred to as "Respondent", under Section 15-I of the Securities and Exchange Board of India Act, 1992 read with Rule 5 of the Securities and Exchange Board of India (Procedure for Holding Inquiry by

Enquiry Officer and Imposing Penalties by the Adjudicating Officer) Rules, 1995. The Impugned Order seeks to impose a penalty of Rs.9 lac under Section 15HA of the Securities and Exchange Board of India Act, 1992 on the Appellant for the alleged violation of Regulations 4(1), 4(2)(a), (b), (e), (g) and (n) of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003, hereinafter referred to as "FUTP Regulations". A further penalty of Rs.1 lac is sought to be imposed on the Appellant by the same Impugned Order for the alleged violation of clauses A(1), A(2), D(1), D(4) and D(5) of the Code of Conduct as specified in Schedule II under Regulation 15 of the Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Regulations, 1992 , 'hereinafter referred to as Broker Regulations.'

2. Brief facts leading up to the present case are that the Respondent initiated an investigation in the scrip of M/s Adani Export Limited, hereinafter referred to as "AEL", which is a public company and has been mainly trading on the two exchanges, BSE and NSE. The investigation appears to be in respect of examining the possibility of violation of various provisions of the FUTP Regulations in respect of their trading in the scrip during the period between July 9, 2004 to July 14, 2004 (first period) and August 8, 2005 to September 9, 2005 (second period). It is stated that during the investigation, the said scrip witnessed wide fluctuations in its price ranging from 481 to 756 during the first period and from Rs.64.35 to Rs.74.20 during the second period. The role

of various brokers and their clients was scrutinized in respect of trading in the scrip of AEL. It appears to be the case of the Respondent that through collusion with brokers and clients, certain entities transacted in the shares of AEL in a manner which led to the creation of artificial volumes in the scrip and, consequently, the projection of a false market. It led to a distorted market equilibrium which was responsible for a spurt in the price of the scrip which did not have any co-relation with the performance of the company. In this connection, the role of the Appellant, a sub-broker was also investigated in respect of trading undertaken by the Appellant at the instance of his client Shri Nitin R. Patel. The Appellant was found to be guilty of violating the FUTP Regulations as well as the Broker Regulations. A show-cause notice was accordingly issued on June 28, 2008 as per the rules and the Appellant submitted its reply to the said show cause notice denying all the allegations against him. The Appellant sought certain additional documents but did not file any supplementary detailed reply.

3. The case of the Appellant is that it is a small time sub-broker and has acted only at the instance of and on behalf of its client, namely, Shri Nitin R. Patel. The Appellant did not have any knowledge of the alleged manipulative intention of said Shri Nitin R. Patel. It is further submitted that the transactions in question were carried out by the Appellant in the normal course of business strictly as per the instructions of its client and on his behalf. In this context, it is argued by Shri Deepak R. Shah, learned counsel for the Appellant, that there is

absolutely no evidence on record to suggest even remotely the possibility that the Appellant had been part of any alleged design of his client, namely, Shri Nitin R. Patel in connivance with others.

4. It is further argued on behalf of the Appellant that the contentions/submissions raised by the Appellant at the time of enquiry have not been considered, while being negatived and even ignored by the Adjudicating Officer while passing the Impugned Order. Although, it is alleged in the show-cause notice that there was reversal of trades amounting to synchronization thereof, no details of such trades have been placed on record or furnished to the Appellant so as to enable the Appellant to effectively respond to the same. The Appellant has also specifically contended in Paragraph 5.12 of the Appeal that there was undue and unexplained delay on the part of the Respondent in concluding the said enquiry which violates the principle of natural justice. It is pointed out by the Appellant that initially an enquiry officer, namely, Ms. M. S. Babita Rayadu, was appointed as the Adjudicating Officer and replaced by one Mr. Sandeep Deore. All this happened between July to November, 2007. Thereafter, a show-cause notice was issued on June 28, 2008 to which the Appellant replied on August 1, 2009. The Appellant has also attended a couple of personal hearings and on February 24, 2010, sought time to file another reply by March 26, 2010 in view of certain additional documents obtained by him from the Adjudicating Officer. However, on scrutiny, it was found that none of the documents pertained to the Appellant and as such he did not find it necessary to prefer any other reply in addition to the one already filed on

August 1, 2009. The Appellant, therefore, submits that the Respondent should have, thereafter, passed the final order within a reasonable time but instead took more than 33 months to pass the Impugned Order against the Appellant imposing the penalty in question. This inordinate delay remains unexplained.

5. Learned counsel for the Appellant has submitted that the reliance placed by the Adjudicating Officer, on the case of Ketan Parekh vs. Securities and Exchange Board of India (Appeal no. 2 of 2004) decided on July 14, 2006 is totally misplaced. Similar is the contention of the Appellant regarding the judgement of the Hon'ble Supreme Court in the case of Securities and Exchange Board of India vs. Shriram Mutual Fund and another (2006)5 SCC 361 reported in AIR 2006 SC 2287. In this connection, it is pointed out by the learned counsel for the Appellant that the penalty on the person who actually dealt in the shares in question i.e. Shri Nitin R. Patel, was Rs.5 lac to begin with and the same was reduced to Rs.2 lac by this Tribunal in Appeal no. 27 of 2012 dated February 21, 2012.

6. Lastly, the Appellant submits that the Respondent has also failed to take into consideration the factors stipulated in Section 15J of the SEBI Act, before levying such a harsh penalty.

7. The present appeal was admitted on March 7, 2013 and the Respondent was afforded an opportunity to file a reply-affidavit within 4 weeks. However, when the matter was taken up for final hearing on the fixed date i.e. April 30, 2013, the Respondent made it clear that it did

not intend to file any reply-affidavit in the matter and as such the appeal was heard, with the consent of the parties, on the basis of records made available by the Appellant in its appeal and the oral submissions advanced by both the parties on fact and applicable law in the matter. The learned counsel for the Respondent, argued that the Appellant had been found guilty of the provisions of the FUTP Regulations as well as the Code of Conduct for Sub-Brokers. The Adjudicating Officer had granted the Appellant reasonable opportunity of defending his case. The Appellant availed of the said opportunity by filing a reply to the show-cause notice as well as by personally attending the hearings scheduled before the Adjudicating Officer. However, it is vehemently argued by the Respondent that the Appellant failed to file a second reply for which he sought time of 30 days or so from the Adjudicating Officer after obtaining certain additional documents and hence the appeal deserves to be dismissed.

8. Both the learned counsel for the parties have been heard at length and the pleadings in the appeal and the documents annexed therewith have been minutely perused.

9. Before analyzing the respective submissions of the parties on merit, the relevant provisions of the FUTP Regulations and Broker Regulations, alongwith other relevant provisions of the SEBI Act, 1992 are reproduced herein below for the sake of convenience:

> ***"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;

...

(e) any act or omission amounting to manipulation of the price of a security;"

...

(g) entering into a transaction in securities without intention of performing it or without intention of change of ownership of such security."
(n) circular transactions in respect of a security entered into between intermediaries in order to increase commission to provide a false appearance of trading in such security or to inflate, depress or cause fluctuations in the price of such security;."

Similarly, Schedule II of the Code of Conduct for Sub-Brokers reads as under:

SCHEDULE II

CODE OF CONDUCT FOR SUB-BROKERS

A. General.

(1) Integrity: A sub-broker, shall maintain high standards of integrity, promptitude and fairness in the conduct of all investment business.
(2) Exercise of due Skill and Care: A sub-broker, shall act with due skill, care and diligence in the conduct of all investment business.

D. Sub-Brokers vis-à-vis Regulatory Authorities

(1) General Conduct: A sub-broker shall not indulge in dishonourable, disgraceful or disorderly or improper conduct on the stock exchange nor shall he willfully obstruct the business of the stock exchange. He shall comply with the rules, bye-laws and regulations of the stock exchange.

(4) Manipulation: A sub-broker shall not indulge in manipulative, fraudulent or deceptive transactions or schemes or spread rumors with a view to distorting market equilibrium or making personal gains.

Sections 15HA, 15HB, 15I & 15J of SEBI Act, 1992 are also reproduced herein below for the sake of convenience:-

"15HA. Penalty for fraudulent and unfair trade practices.

If any person indulges in fraudulent and unfair trade practices relating to securities, he shall be liable to a penalty not exceeding twenty-five crore rupees or three times the amount of profits made out of such practices, whichever is higher."

15HB. Penalty for contravention where no separate penalty has been provided.-

Whoever fails to comply with any provision of this Act, the rules or the regulations made or directions issued by the Board thereunder for which no separate penalty has been provided, shall be liable to a penalty which may extend to one crore rupees.

15-I Power to adjudicate- *(1) For the purpose of adjudging under sections 15-A, 15-B, 15-C, 15-D, 15-E, 15-F, 15-G [,15-H, 15-HA and 15-HB], the Board shall appoint any officer not below the rank of a Division Chief to be an adjudicating officer for holding an inquiry in the prescribed manner after giving any person concerned a reasonable opportunity of being heard for the purpose of imposing any penalty.*
(2) While holding an inquiry the adjudicating officer shall have power to summon and enforce the attendance of any person acquainted with the facts and circumstances of the case to give evidence or to produce any document which in the opinion of the adjudicating officer, may be useful for or relevant to the subject matter of the inquiry and if, on such inquiry, he is satisfied that the person has failed to comply with the provisions of any of the sections specified in sub-section (1), he may impose such penalty as he thinks fit in accordance with the provisions of any of those sections.

"15J- Factors to be taken into account by the adjudicating officer

While adjudging quantum of penalty under section 15-I, the adjudicating officer shall have due regard to the following factors, namely:-

(a) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default;

(b) the amount of loss caused to an investor or group of investors as a result of the default;

(c) the repetitive nature of the default."

10. First, we deal with the Respondent's emphatic contention that the Appellant did not file a second reply despite the fact that it sought, and received, time till March 26, 2012 to reply to the additional documents provided to it by the Respondent. At the outset, the Tribunal notes that the Appellant's failure to submit a second reply to the show-cause notice, after having obtained additional documents from the Adjudicating Officer, would not in itself amount to violation of the FUTP Regulations in question. There has to be sufficient material and evidence to arrive at such an inference against the Appellant, which cannot be based on flimsy grounds. It has been clearly pointed out by the learned counsel for the Appellant that after filing a reply on September 1, 2009 to the show-cause notice, no need was felt to file additionally a detailed reply in as much as the additional documents furnished by the Inquiry Officer pertained to Shri Nitin R. Patel and not the Appellant. In this connection, the Tribunal notes that even the points raised by the Appellant in the first reply dated September 1, 2009 have not been considered by the Adjudicating Officer while passing the Impugned Order. Therefore, this submission of the Respondent does not

add any value to their case. Even observations / findings of the Adjudicating Officer in paragraphs 11 to 15 of the Impugned Order are based on some investigation report issued while blindsiding the Appellant. There is no evidence on record to substantiate the allegations levelled against the Appellant.

11. We now deal with the main issue regarding whether or not the Appellant has violated Regulations 4(1) and 4(2),(a),(b),(e),(g) and (n) of the FUTP Regulations, 2003. Regulation 4(1), as reproduced above, provides that no person shall indulge in fraudulent and unfair trade practice in securities. Regulation 4(2) provides that dealing in securities shall be deemed to be fraudulent and an unfair trade practice if it involves fraud and may include all or any of the ingredients enumerated in sub-sections (a),(b),(e),(g), and (n) of Regulation 4(2). Regulation 4(2)(a) deals with an act which creates a false impression with respect to trading in the securities market. Regulation 4(2)(b) deals with a situation where the securities are not intended to be transferred but operate only as a device to inflate or depress the price of such securities for wrongful gain or avoidance of loss. Regulation 4(2)(e) deals with manipulation of the price of a security. Regulation 4(2)(g) deals with transactions which are not intended to be performed by taking them to their logical conclusion. Similarly, Regulation 4(2)(n) prohibits circular transactions between intermediaries which are mainly intended to increase commission and also to provide a false appearance of trading in that

security. Paras 12 to 15 of the Impugned Order deal with the allegedly manipulative way in which the trades in question were synchronized.

> "12. During the course of the said investigation, it was observed that the Noticee was one of the sub-brokers who had traded substantially in the scrip of AEL during the first and the second period for the said client. The Noticee, for the said client, has allegedly executed synchronized trades for 1,15,870 shares of AEL during the period from July 9, 2004 to July 27, 2004. Further, the said client also entered into self trades for 52,910 shares. The said client also entered into structured trades wherein he reversed the trades with particular clients of other brokers. A total trading of 1,29,422 shares was executed by the said client in such manner between July 16, 2004 and July 27, 2004. This quantity accounted for 12.5% of the total traded quantity during this period. It is further observed that during the period between July 28, 2004 to January 14, 2005 the said client is alleged to have entered synchronized trading for buying 83,45,924 shares and selling 87,60,410 shares. The said client was part of the group which executed trades of 3,48,53,139 shares during the above period which is around 51% of total traded volumes. Of these trades 3,04,68,762 shares (87.39 % of their trades) appear to be synchronized.
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> 13. It is further alleged that the said client along with few other entities executed reverse trades to the extent of 38,21,269 shares during the second period. It is alleged that the said client along with few other entities traded in a manner such that orders for 28,22,240 shares appear to be synchronized as the buy and sell orders were placed within time gap of 1 Page 6 of 12 minute. Moreover, for 18,38,077 shares buy and sell order quantity and rate identical and placed within a time gap of 1 minute from each other. In case of 116 trades for 2183102 shares the time gap between the buy and sell orders was between 0-10 seconds. The said client's contribution to the alleged manipulation is to the extent of 13,21,582 shares on buy side and 15,04,408 on the sell side. Similarly on NSE, for the same period the said client has allegedly entered into synchronized trades to the extent of 12,25,260 shares.
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> 14. It is alleged that the said trades were synchronized as the buy and sell orders were placed within time gap of 1

> minute with negligible or no price difference. Further, these trades have been reversed on the same day. These trades were allegedly done with a view to increase the price of the scrip and create artificial volumes and consequently create artificial demand in the scrip. It is further alleged that the Noticee, by executing the said trades on behalf of the said client, had aided and facilitated manipulation in the scrip. This allegation is substantiated by the fact that the said client was doing trading in huge volume and was reversing it on the same day. There has been negligible change in the beneficial ownership because of the trading done by the said client and the trading done by said client has only contributed to the increase in the price and volume of the scrip of AEL. The orders placed by the said client used to be identical in terms of price and quantity and used to be placed with negligible price difference.
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> 15. In response of the said allegation of structured trades, the Noticee submitted that the said transactions were carried out by the client in normal course of business and there is nothing on record to show that the Noticee had knowledge of manipulative intention of the said client. Further, synchronized trading and reversal trading are not illegal per se."

12. Thus, a perusal of the above stated provisions of Regulation 4 and its sub-regulations reveals that the allegation of fraud can be levelled against a person/entity only for good reasons and on the basis of clear and unambiguous evidence. Such an allegation of fraud may shake the very foundation of the business of the entity in question and may adversely affect the same. Therefore, the onerous task of proving such a serious allegation lies on the person levelling such accusation on the basis of preponderance of probability. A minute reading of the Adjudicating Officer's Impugned Order dated December 14, 2012 does not demonstrate the manner in which the Appellant's actions have led to the creation of a false market and the basis on which the Appellant has

been condemned for the commission of fraud, that too in connivance with others. No evidence has been brought on record to establish a connection between the Appellant and the alleged fraudulent transactions undertaken by Shri Nitin R. Patel. It is a matter of record that the alleged default is the first and only aspersion cast on the Appellant with respect to its business and, heretofore, has not had any of its acts called into question by any authority, regulatory or otherwise. Moreover, it is evident from the Impugned Order that the Appellant has enjoyed no unfair advantage or benefit of any nature owing to the execution of the trades in question, nor have the same resulted in any kind of loss suffered by investors in the scrip of AEL. This is evident from the fact that the Respondent has not received any complaint with respect to any of the allegedly manipulative acts of the Appellant.

13. The Appellant, as is evident from the record, acted only as a sub-broker, who is at a lower rung in the hierarchy of brokers, as above him stand the broker and the stock exchange. We agree with the Appellant in that it is an inconsequentially small market player earning a meager amount every year and can in no way be placed at par with other dominant entities executing numerous transactions in the securities market on a regular basis. We further observe that the entire Impugned Order seems to be based on mere presumptions. In paragraph 16 of the Impugned Order, after relying upon Ketan Parekh's judgement of this Tribunal, the Adjudicating Officer proceeds to observe as under:-

> 16. …..
>
> It is observed that the trading done by the said client was huge and the Noticee should have been

> alarmed by the trading being executed by the client. Even if the client was doing day trading, such pattern of trading still remains unexplained. The said client had entered the orders with precise timing, quantity and price. Such preciseness could not be achieved unless there is an understanding between the Noticee and the said client. The face that the said client has reversed his trading and has entered into self trades shows that the clients activities could not be considered to be normal by any prudent standard. Further, the Noticee has failed to submit any detailed submissions in response to SCN even after providing it with all the necessary materials and providing it adequate opportunities.
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> 17. In view of the above observations, findings and material on record I conclude that the allegation of violation of Regulation 4 (1) and 4 (2) (a), (b),(e),(g) and (n) of the PFUTP Regulations, 2003 by the Noticee is proved."

The above said finding is, in our opinion, totally perverse in law since no valid basis has been put forth through documentary evidence or through witnesses to substantiate such deemed nexus of the Appellant with the fraudulent acts of Shri Nitin R. Patel. All that can be inferred from the above-stated findings of the Respondent is that the client, Shri Nitin R. Patel, executed trades which were perfectly timed to cause manipulation in the price of the scrip of AEL. How this particular action of the client leads to the conclusion that the Appellant and Shri Nitin R. Patel acted in collusion with each other to create a false market with respect to the shares of AEL has, in our considered opinion, not been demonstrated with any degree of clarity by the Adjudicating Officer in the Impugned Order.

14. At this stage, we may revert to the reliance placed by the Appellant on the case of Shri Nitin R. Patel, decided by this Tribunal on

February 21, 2012. In this matter, the Respondent investigated trades executed in the scrip of AEL during the periods between July 9, 2004 and January 14, 2005 and between August 1, 2005 and September 5, 2005. These trades were executed by Shri Nitin R. Patel, through Ess Ess Intermediaries, the Appellant in the instant case. The Respondent's case was that Shri Nitin R. Patel had executed circular and reversal trades thereby generating huge artificial volumes of shares leading to manipulation in the price of the scrip of AEL. Being satisfied of his guilt, the Respondent levied a penalty of Rs. 5 lac on Shri Nitin R. Patel. Shri Nitin R. Patel, being aggrieved by the Respondent's order approached this Tribunal denying the allegations of circular trading while stating that several other entities had traded in the scrip of AEL and the Respondent had passed orders against all these entities merely to the tune of Rs.1 lac. This Tribunal, while holding that the facts regarding self trading and circular trading stood established, decreased the penalty levied on Shri Nitin R. Patel to Rs. 2 lac. It is pertinent to reproduce para 5 of the judgement delivered by Hon'ble Shri S.S.N. Moorthy:-

> "5. We have considered the rival arguments. We have also gone through the order of the adjudicating officer in the case of Mahesh Kumar A. Panchal and those in respect of other individuals cited by the appellant's learned counsel. The fact of synchronised trades and self trades stands established. The appellant's learned counsel has not brought on record any material to disprove the manipulations established by the adjudicating officer. The adjudicating officer has observed that the appellant entered into synchronized trades to the extent of 58,010 shares on the buy side and 57,860 shares on the sell side during the period 9.7.2004 and 27.7.2004. Out of the above 52,910 shares were traded fictitiously as he was the client on the buy side as well as the sell side and the orders were synchronized.

> During the period 16.7.2004 to 27.7.2004, the appellant entered into trades for 1,29,422 shares, orders for which were synchronized as the buy and sell orders were placed within a gap of one minute. Similarly during the period 28.7.2004 and 14.1.2005, the appellant indulged in reversal of trades by placing orders for 3,04,68,962 shares which were synchronized. The adjudicating officer has extensively dealt with similar instances. So the appellant's violation in respect of synchronized trades and self trades stands established. However, there is merit in the contention of the appellant's learned counsel that the quantum of penalty is on the higher side when the penalty imposed in the case of similarly placed market operators dealing in the scrip of the company is taken into account. Even though penalty provisions cannot be straight jacketed to fall within strict parameters they should be commensurate with the gravity of the violation and other attendant circumstances. It goes without saying that the facts and circumstances of each case have to be viewed in their proper perspective."

15. It is evident from the records that the Appellant acted solely on the behest of its client, Shri Nitin R. Patel, while trading in the shares of AEL. As stated above, while pronouncing its decision in the matter of Nitin R. Patel, this Tribunal observed that the quantum of penalty levied upon transgressors of the law under similar circumstances should be commensurate with the gravity of the act which leads to deviation from the provisions of law. Now, the fact of the matter is that Shri Nitin R. Patel, along with other market operators which dealt in the scrip of AEL, has been penalised to the extent of Rs. 2 lac, while the sub-broker Appellant has been asked to pay a totally unwarranted penalty of Rs. 9 lac in the facts and circumstances of the case analysed in detail hereinabove. In the opinion of this Tribunal, to a reasonable mind, the facts of this matter speak for themselves. As pointed out earlier, no evidence has been adduced to demonstrate any sort of collusion between

the Appellant and Shri Nitin R. Patel while dealing in the scrip of AEL, with the intention to manipulate the price of the scrip. However, we do believe that the Appellant as a sub-broker should have been more vigilant while executing the trades in question. Even as a small-time sub-broker, the Appellant has the task of remaining alert at all times without taking its clients at face value. Unless the Appellant appreciates this duty as its paramount obligation, clients such as Shri Nitin R. Patel will keep trying to make profits at the expense of innocent investors caught unawares in the unethical scheme of such clients in the capital market and the Respondent, as a responsible Regulator, has rightly called upon the Appellant to pay a nominal amount of Rs. 1 lac for this inadvertence. Therefore, keeping the above said in mind, this Tribunal is inclined to do away with the penalty of Rs. 9 lac imposed upon the Appellant for the alleged violation of the FUTP Regulations, 2003 while upholding that of Rs. 1 lac for the violation of the Code of Conduct as specified in Schedule II under Regulation 15 of the Broker Regulations. This appeal, to the aforesaid extent, stands partly allowed. No order as to costs.

Sd/-
Jog Singh
Member &
Presiding Officer *(Offg.)*

19.06.2013
Pk