BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Date of Hearing : 09.04.2014

Date of Decision : 23.04.2014

Appeal No. 20 of 2014

Ms. Pooja Menghani
5-24, Old Rajender Nagar,
New Delhi – 110 060. …Appellant

Versus

Securities and Exchange Board of India
SEBI Bhavan, Plot No. C4-A,
G-Block, Bandra Kurla Complex,
Mumbai – 400 051. …Respondent

Mr. M.P. Rao, Senior Advocate with Mr. Ramesh Mishra, Company Secretary in Practice for the Appellant.

Mr. Shiraz Rustomjee, Senior Advocate with Mr. Mihir Mody and Mr. Pratham V. Masurekar, Advocates for the Respondent.

CORAM : Justice J. P. Devadhar, Presiding Officer
Jog Singh, Member
A. S. Lamba, Member

Per : Jog Singh

The present appeal is preferred by the appellant against the impugned order dated April 30, 2012 by which she has been found to be guilty of indulging into fraudulent and unfair trades in respect of few companies. The appellant is alleged to have resorted to “front-running” to earn ill-gotten profits by the trades in question. She is stated to have earned approximately ₹ 49 lac in an unlawful manner. The learned Adjudicating Officer, hereinafter referred to as “AO”, has found the appellant guilty of violating

the provisions of Regulations 3(a), (b), (c), (d) and 4(1) of the SEBI (Prohibition of Fraudulent and Unfair Trades Practices Relating to Securities Market) Regulations, 2003 (for short FUTP Regulations). Consequently, a penalty of ₹ 1 crore has been imposed on the appellant under Section 15HA of the SEBI Act, 1992, which prescribes a penalty of ₹ 25 crore or three times the illegal profits earned by a person by violating the law, whichever is higher.

2. Briefly stated, the facts of the case are that respondent SEBI conducted an investigation in the trading of appellant for the period from June 1, 2008 to January 12, 2009 and noticed irregularities in her dealings in the scrips of four companies, namely, Amtek Auto Ltd. (Amtek Auto), Amtek India Ltd. (Amtek India), Monnet Ispat Ltd. (Monnet Ispat), Ahmednagar Forgings Ltd. (Ahmednagar Forging). She dealt with in these scrips through brokers, namely, Religare Securities Ltd. (Religare), ISF Securities Ltd. (ISF), India Infoline Securities Ltd. (India Infoline), Narayan Securities Pvt. Ltd. (Narayan). Other entities who dealt with the same scrips are Live Star Marketing Pvt. Ltd. (Live Star), SRS Portfolio Ltd. (SRS) and MSR Marketing Pvt. Ltd. (MSR).

3. On the investigation a general trend of trading was noticed on behalf of the appellant quo other parties which *prima-facie* revealed that the appellant had always been trading in the four scrips in question ahead of Live Star, SRS and MSR with prior knowledge of the buy orders of the aforesaid entities and, thus, indulged in front-running. This modus operandi adopted by the appellant has been found to be violative of the various provisions of the FUTP Regulations as mentioned hereinabove.

4. A show cause notice dated June 20, 2011 was, accordingly, issued to the appellant and enquiry was conducted in terms of Rule 3 etc. of the SEBI (Procedure of Holding Enquiry and Imposing Penalties by the Adjudicating Officer) Rules, 1995 (for short Adjudication Rules). The appellant personally appeared before the adjudicating officer and availed of the opportunity of filing reply / written submissions too. She also appointed an Authorized Representative, namely, M. G. Associates, Advocates & Solicitors, to represent her interest before the learned AO. Said Authorized Representative filed exhaustive reply / written submissions before the learned AO denying the charges. It was, interalia, submitted on behalf of the appellant that she was a random and innocent investor and was relying on her own competence, instinct and insinuation before entering into the dealings. Her investments in the scrips were based on information received from the market as well as from her brokers. It was, therefore, contended that no charge of front-running was made out against her. It is further argued that matching of large number of sell orders of the appellant with the buy orders of the opposite parties were a mere coincidence.

5. The learned AO after holding enquiry and considering the material brought before him including statement / cross-examination, reply / written submissions of the appellant came to the conclusion that the appellant colluded with Mr. Deepak Khurana of Religare to obtain sensitive information regarding forthcoming orders from MSR, SRS and Live Star and thereby indulged in front-running on that basis. This is how she is found to have earned huge illegal profits to the tune of about ₹ 49 lacs by playing a fraud upon the market and at the cost of bonafide investors. This act of the appellant has seriously undermined the market integrity. The admitted income of the appellant ranged between ₹ 5 lac to ₹ 10 lac per

annum but she took huge positions in the scrips of the four companies in question running up to ₹ 10 to ₹ 12 crore. The trades, therefore, undertaken by the appellant based on prior information where held to be in violation of FUTP Regulations as the same were found to be manipulative and deceptive tradings tantamounting to front-running.

6. In this background, the impugned order dated April 30, 2012 has come to be passed against the appellant and the same is the subject matter of adjudication before this Tribunal.

7. We have heard the learned counsel for the parties at length and have perused the pleadings minutely. Shri M. P. Rao, learned senior counsel who appeared on behalf of the appellant mainly argued that the appellant traded in the scrips of four companies in question based on her own technical analysis. She had studied these scrips for long time and the same being fundamentally strong companies, the appellant was motivated to invest in these scrips. Shri Rao further submitted that role of other buyers has not been investigated by the respondent SEBI and the appellant cannot be said to have indulged in front-running all alone. It was suggested by Shri Rao that atleast two parties are required to be there to complete an offence of front-running, if any. SEBI has not enquired into role of brokers or other buyers, therefore, the whole adjudication proceedings are vitiated. On the other hand, the learned senior counsel for the respondent Shri Rustomjee vehemently argued and defended the order. He has submitted that factual data and analysis of trades undertaken by the appellant in respect of each of the four companies have been thoroughly analyzed by the respondent before coming to the conclusion that appellant resorted to front-running and thereby earned profit to the tune of approximately ₹ 49 lacs. It is

undoubtedly an unscrupulous practice and clearly barred by the FUTP Regulations.

8. The Appellant's main assertion that she traded in the four scrips in question on the basis of her own analysis of the fundamentals of the four companies is totally misconceived and belied by the specific findings of learned AO in respect of each of the four scrips. In respect of Amtek Auto the appellant traded in the shares through Religare for 15 days. She bought 3,69,954 shares and sold 3,69,914 shares. Out of the 15 days, on 14th days the appellant squared off her position at the end of each day. On the basis of detailed factual analysis of the trade done by the appellant in respect of Amtek Auto, learned AO at pages 9 and 10 (internal) of the impugned order came to the conclusion that on the days when the appellant's sell orders matched with the buy orders of MSR, she had invariably bought shares at lower prices prior to the buy orders of MSR.

9. This phenomenon has happened on days together and hence it cannot be said to be a coincidence as contended by Shri Rao, the learned senior counsel for the appellant. Similarly, the net profit of Amtek Auto for the quarter ending September 30, 2008 was substantially reduced to ₹ 4806 lac from ₹ 7497 lac achieved in the preceding quarter ending June 30, 2008. This fact clearly contradicts the appellant's contention that she traded in the scrips of the four companies because they were fundamentally strong. This is a hollow submission, rather an afterthought, and hence, repelled. Such findings are clearly to be noted in respect of the remaining three scrips of the companies in question in the impugned order itself. Argument of Appellant that investments were made on account of fundamentals of those companies being strong cannot be accepted because ordinarily where fundamentals of a company are strong, long term investments are made and

not by way of purchasing and selling the shares on the same day. Therefore no fault can be found with the Adjudicating Officer in rejecting the contention of the Appellant that investments were made on account of strong fundamentals of the companies in question.

10. Moreover, it is an admitted position that appellant and Shri Deepak Khurana of Religare (Head of Pitampura Branch, Delhi of Religare) had telephonic conversation on every morning whereafter appellant undertook trades in question. Appellant has herself admitted that she used to call Shri Deepak Khurana in the evening and used to instruct him to call her on the next day morning so that she could undertake trades in the scrips. Admittedly Deepak Khurana used to place buy orders on behalf of MSR, SRS and Live Star at a higher price and after the telephonic conversation with Deepak Khurana, appellant used to place sell orders at a price nearer to the price at which buy orders were placed by Deepak Khurana on behalf of MSR, SRS and Live Star. Therefore, the charge of front-running brought home by the learned AO qua the appellant cannot be said to be ill-founded and in fact there is sufficient material to prove the same. As far as other persons connected in the trades in question executed by the appellant, like Shri Deepak Khurana etc., SEBI ought to have taken appropriate action against them as per law. During the course of arguments, it was brought to our notice by Shri Rustomjee, learned senior counsel for the respondent that SEBI had already initiated appropriate proceedings against Shri Deepak Khurana.

11. Front-running is undoubtedly very injurious to the market and which is resorted to by some unscrupulous persons at the cost of innocent and genuine investors who incidentally or unfortunately do not possess that information which such front runners have come to know due to any means

or by their position. As per Black's Law Dictionary (9th Edition) by Bryan A. Garner the concept of front running is defined as :-

> *"A broker's or analyst's use of nonpublic information to acquire securities or enter into options or futures contracts for his or her own benefit, knowing that when the information becomes public, the price of the securities will change in a predictable manner. This practice is illegal. Front-running can occur in many ways. For example, a broker or analyst who works for a brokerage firm may buy shares in a company that the firm is about to recommend as a strong buy or in which the firm is planning to buy a large block of shares."*

12. Lastly, The mischief of front-running, apart from being fraudulent and manipulative in nature is almost akin to the offence of insider trading wherein also someone is in advantageous position and hence in possession of certain information which he or she has come to know before others can do so. In FUTP Regulations, front-running is not mentioned as such but every such activity is condemned and is treated as a fraud on the market. Regulations 3(a), (b), (c), (d) and 4(1) of FUTP Regulations are relevant and reproduced hereinbelow :-

Prohibition of certain dealings in securities

"3. 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 thereunder;

(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 thereunder."

"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."

13. Similarly, the definition of expression "fraud" as envisaged by Regulation 2(1)(c) of the FUTP Regulations is wide enough to cover the mischief of "front-running". Regulation 2(1)(c) reads as under:

> "2(1)(c) "fraud" includes any act, expression, omission or concealment committed whether in a deceitful manner or not by a person or by any other person with his connivance or by his agent to deal in securities, whether or not there is any wrongful gain or avoidance of any loss, ……."

14. As far as quantum of penalty is concerned, Section 15-HA of the SEBI Act, prescribes penalty not exceeding ₹ 25 crore or three times the amount of profits made by such fraudulent and unfair trade practices, whichever is higher. Therefore, penalty of ₹ 1 crore imposed on the appellant which is even less than three times the profit of ₹ 49 lac made by the appellant in an illegal manner does not require any interference of this Tribunal.

15. In view of above discussion of law and fact, we do not find any illegality in the impugned order and same is hereby upheld. The appeal is, accordingly, dismissed with no order as to costs.

Sd/-
Justice J. P. Devadhar
Presiding Officer

Sd/-
Jog Singh
Member

23.04.2014
Prepared and compared by:
PTM/RHN

Per : A.S. Lamba

1. This appeal has been filed by Pooja Menghani (hereinafter referred to as “Appellant”) against Securities and Exchange Board of India (hereinafter referred to as “Respondent”) against Adjudication Order No. PB/AO-36/2012 dated April 30, 2012 holding Appellant violative of Regulations 3(a), (b), (c), (d) and 4(1) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (hereinafter referred to as “PFUTP Regulations”) during June 1, 2008 to January 12, 2009 (“Investigation Period” or “IP”) and consequently liable to penalty under Section 15HA of SEBI Act, 1992 (hereinafter referred to as “SEBI Act”).

2. A Show Cause Notice (“SCN”) was issued to Appellant on June 20, 2011, in which it was alleged that Appellant had bought and sold equal quantities of shares in large volumes in four scrips, namely Amtek Auto Ltd., Amtek India Ltd., Monnet Ispat Ltd. and Ahmednagar Forgings Ltd. through Religare Securities Ltd. (“Religare”) ISF Securities Ltd. (“ISF”), India Infoline Securities Ltd. (“India Infoline”), Narayan Securities Pvt. Ltd. (“Narayan”); and that Appellant traded above scrips ahead of Live Star Marketing Pvt. Ltd. (“Live Star”), SRS Portfolio Ltd. (“SRS”) and MSR Marketing Pvt. Ltd. (“MSR”), with prior knowledge of buy orders from Live Star, SRS and MSR, in these four scrips and did front running in said scrips, which resulted in violation of provisions of Regulations 3(a), (b), (c), (d) and 4(1) of PFUTP Regulations.

3. Appellant replied to SCN as following:

- ❖ Appellant was introduced by Deepak Khurana to Religare and he might have passed on some advance information to Appellant, which turned out to be lucrative.

- ❖ There is nothing on record to substantiate allegations of violation of PFUTP Regulations against Appellant. Appellant was a random and innocent investor and was relying on her own competence, instincts or intuition before entering into the deals.

- ❖ Appellant did not defy any norms or submitted wrong financials to the company.

- ❖ Appellant went through KYC norms and it was for Religare to ensure and decide to whom to extend credit or not.

- ❖ Statements of Appellant and Deepak Khurana were recorded and there is no contradiction between the two statements.

- ❖ Deepak Khurana and Appellant met during KYC norms and was nothing personal between the two.

- ❖ Religare has not found anything amiss with conduct of Deepak Khurana or that Deepak Khurana extended any favours to Appellant.

- ❖ There is nothing on record to prove that Appellant rigged the deals.

- ❖ Matching of buy order with that of another broker's sale order could be a matter of chance, coincidence or matching sale / purchase order by buyer or seller as is obvious from the net. Religare was buyer's as well as seller's broker in Ahmednagar Forging and Amtek Auto, which proves Religare would not side / pitch one investor against the other investor.

- ❖ There was no intention to commit any fraud by Appellant and that there was no connivance with the broker or the investee company resulting into extraordinary gains.

4. Facts of the case in brief are that Appellant was purchasing some quantity of shares in four scrips mentioned in paragraph 2 above and put up the same for sale on the same day, during IP, and sale order was almost at the same time of the day, when one of three entities, namely, Live Star, SRS or MSR will enter a purchase order for the same scrip for most of the sale quantity or entire quantity offered in sell order or very slightly lesser quantity than sale quantity but price at which buy order is placed will be higher a little or substantially higher than Last Trading Price (LTP) of the scrip at the time of placing of buy order by Live Star, SRS or MSR; resulting in trade between Appellant and buyers, with net positive for the Appellant.

5. It may be mentioned that purchase price of four scrips by Appellant in question has not been mentioned in impugned order, but from (impugned

order page 31 of 32) total buy value of individual of four scrips, under consideration, has been mentioned, alongwith sale value of these four scrips during IP, which shows that Appellant made profit of Rs. 49,05,832/- on total buy value of these scrip of Rs. 11,09,37,611/-, in buy and subsequent sale of four scrips by Appellant to three buyers, during IP. It is also seen that Appellant was trading in security market through four brokers namely, India Infoline, Narayan, Religare and ISF, while purchasers of the four scrips by buyers namely, Live Star, SRS, MSR is through Sunglow and Religare only.

6. Since price at which Appellant purchased the four scrips has not mentioned, yet it can be safely inferred from perusal of impugned order that Appellant made handsome profit on each and every of her purchase in these four scrips and subsequent sale of scrip, on the day of purchase itself, to one of the buyers during IP, when purchasers was one of the three buyers only and that Appellant purchased these scrips, to begin with, at lower price than her sale price.

7. Since the case in question, is of front running where it is alleged that Appellant was in knowledge of buy orders of three buyers, in advance, Appellant will purchase the scrip, in question, in advance and make money through sale of same subsequently to one of three purchasers at higher price than Appellant’s purchases; it is important that role of each and every brokers alongwith role of three purchasers, associated with impugned trade is investigated, but role of only Religare has been investigated. Role of other brokers is also essential, since broker namely, Sunglow, figures in substantial numbers of purchases by three purchasers and other brokers, namely India Infoline, ISF and Narayan figure in significant number of trades for buy by Appellant, although, it is not mentioned as to who was the

broker / brokers for Appellant for her sale trades, but it may be safe to presume that sale broker for Appellant was the same buy broker, since, Appellant is a day trader only and Appellant's trades are not delivery based.

8. From various facts and figures mentioned in impugned order and SCN and arguments / findings recorded by Ld. Adjudicating Officer, it is clear, without any doubts, that Appellant was aware of trade of Live Star, SRS and MSR, in advance, so it could position itself in advance with counter-trade of Live Star, SRS and MSR and pricing and timing of her sale trade was designed in such a manner that it could almost complete it's trade during the day of purchase, with net positive, in all trades, with three counterparties during IP.

9. However, entire case-record and arguments of Ld. Counsel for Appellant and Respondent; leaves a lot of questions answered, which make upholding of penalty against Appellant, in isolation, difficult, though it has been proved that it had violated Regulations 3(a), (b), (c), (d) and 4(1) of PFUTP Regulations, which are dealt below:

(i) Price at which Appellant purchased scrips, in question, during IP, has not been mentioned;

(ii) Action taken against other brokers, besides Religare, has not been mentioned;

(iii) The most important aspect that has been entirely missed in impugned case, is complete non-action against the most relevant and important entities i.e. buy clients, namely Live Star, SRS and MSR. As a matter of fact, impugned case,

attempts to show / prove connivance of Appellant and Religare (broker) for the allegedly front running and violation of PFUTP Regulations and have completely ignored role of these three buyers, namely Live Star, SRS and MSR. As a matter of fact, it is not clear from case record as to what was the profession of these buyers. To a query from Tribunal to Ld. Counsel for Respondent, it came to light that these three buyers are “institutional investors”.

(iv) The fundamental of front running is deal / understanding between seller and buyer, either directly or indirectly by through brokers; but for front running to take place, the connivance is between seller and buyer, since these are two relevant entities who have to come to understanding, directly or through brokers, in advance, as to what scrip is to be sold / bought, what price the same will be transacted and what sale price seller has to quote and what price buyer has to quote, what time the seller has to put in its trade in market and what time buyer will put in its trade in market and most importantly the timing of sale / purchase by seller / buyer, which has to be fine-tuned, so that buyers purchases from intended seller only, to exclusion of all other sellers in the market.

(v) In the present case all the above elements were finely matched between sellers (Appellant) and the three buyers, either directly or through brokers, and hence the impugned trades took place between seller (Appellant) and the three buyers.

(vi) However, one most important aspect of front running is of pricing of sell / buy order, which has to be so matched, that it results in profit to seller (Appellant), which has been the fact in impugned case.

(vii) In this context it may be added that seller (Appellant) was placing sale order at price higher than LTP of that time and all three buyers were placing buy order in a range, and highest of range was almost matching with sale price of Appellant, resulting in trade between, Appellant and one of the three buyers, namely Live Star, SRS and MSR, due to matching of timings of sale / buy orders, resulting in net positive for seller.

(viii) It may also be stated that it will not be front running if the trade does not result in positive net for seller, to exclusion of all other sellers in the market and this is possible, if all other elements of trade match which are scrip, stock exchange, timing, price and quantity match and are fine-tuned. Quantity can be different between buy / sale order but generally sale quantity is more or less covered by purchase orders.

(ix) It has also been observed that buyers in front running are generally institutional investors, such as mutual funds etc., whose managers deal with investors and it will be appropriate to investigate as to who are the persons indulging in front running on behalf of buyers – who are placing orders at prices higher than LTP and making sellers of security richer, unduly, in the process. The managers of these institutional investors

are taking the investors in these and institutes for a ride and unscrupulously depriving them of their legitimate profits / gains from investing in mutual funds or with institutional investors.

(x) There is another element which has been overlooked in the present case i.e. scrutiny of bank account of Appellant. While it has been computed that Appellant made a profit of Rs. 49,05,832/- in its trade in four scrips during IP, it would have been relevant to find out as to how much of this profit was reflected in his accounts and how much went to other entities, connected with its trade. It must be mentioned that it would have of great interest to Ld. Adjudicating Officer / investigation to find out, how this profit was shared or it remained with Appellant. If Appellant account had been scrutinized, others profiting from Appellant's undue gains in these trades, would have been brought out.

(xi) Another aspect that has not been brought out in SCN or impugned order is regarding margins money taken by various brokers from Appellant for its trades during IP. Since it appears that trading of Appellant during IP on day it traded, was in vicinity of Rs. 30-40 lakh / day and was this trading covered by margin money provided by Appellant to brokers.

(xii) The last and the most important point regarding the case is seller / buyer are the two components of "front running" and one cannot succeed without involvement / connivance of

other, although these two components may work directly with each other or indirectly through broker / brokers, yet it is a complicity of the two (buyer and seller) and one cannot be held violative of PFUTP Regulations, while other is not proceeded with, at all. In instant case Appellant and broker (Religare) are projected to be conniving parties to the exclusion of three buyers, namely, Live Star, SRS and MSR and other brokers and these three buyers are in fact the conniving parties with Appellant and are responsible to their investors and are doing considerably larger damage to investor's confidence and destabilizing the security markets than Appellant and hence cannot and should not be left out, by showing conniving party to be Appellant and one broker (Religare), to exclusion of all other four brokers and three buyers.

10. In the circumstances, the impugned order dated April 30, 2012, imposing penalty of Rs. 1,00,00,000/- on Appellant under Section 15HA of SEBI Act, for violation of Regulation 3(a), (b), (c), (d) and 4(1) of PFUTP Regulations, is set aside. No costs.

Sd/-
A.S. Lamba
Member

23.04.2014
Prepared and compared by:
msb