Sebi Vs. Manoj J. Doshi

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Court : SEBI Securities and Exchange Board of India or Securities Appellate Tribunal SAT

Decided On : Oct-21-2003

Judge : A Batra

Appellant : Sebi

Respondent : Manoj J. Doshi

Judgement :

1.0 Manoj J. Doshi (hereinafter referred to as "the said broker") is a Stock Broker registered with the Securities and Exchange Board of India (hereinafter referred to as "SEBI") under certificate of Registration No. INB230649317 and a member of the National Stock Exchange of India (hereinafter referred to as "NSE") and having his office at 403A, Dalamal Chambers, 29, New Marine Lines, Mumbai 400 020.

1.1 M/s Morepen Hotels Ltd. (hereinafter referred to as "MHL") is a company incorporated under the Companies Act, 1956 and the shares of MHL are listed at Jaipur Stock Exchange (JSE), Ludhiana stock Exchange (LSE), Delhi Stock Exchange (DSE), National Stock Exchange (NSE) and The Stock Exchange, Mumbai (BSE).

1.2 A major spurt in the volumes and price of the scrip of MHL was observed during the period August to November 2000. SEBI conducted a detailed investigation into the matter and came to the following prima facie findings : 1.2.1 The shares of MHL are closely held and the scrip was initially illiquid.

1.2.2 The spurt in trading in the scrip was confined to BSE and NSE where the volume and price movement were in tandem. There was a little or no trading on the other stock exchanges on which the scrip was listed.

1.2.3 The clients of the said broker had acted in concert with connected persons and indulged in circular trading to give an appearance of trading in the scrip.

2.0 In view of the above findings, SEBI, vide order dated 18.02.2002, appointed an Enquiry Officer under the SEBI (Stock Brokers and Sub Brokers) Regulations, 1992 (hereinafter referred to as "Broker Regulations") to hold an enquiry into the affairs of the said broker in his dealings in the scrip of MHL and possible violations of the rules, byelaws and regulations of NSE, provisions of SEBI Act, 1992, Broker Regulations and the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995 (hereinafter referred to as "FUTP Regulations").

2.1 The Enquiry Officer issued a show cause notice vide letter dated 20.03.2002 advising them to furnish a reply to the allegation that they had failed in discharging in a diligent manner the responsibility undertaken by him and they failed to exercise due skill and care in his dealings in the scrip of Morepan Hotels Ltd. and that they also aided and abetted the clients in creating a false and misleading market in the scrip.

2.2 The broker submitted his reply vide letter dated 21.08.2002. The said broker was also granted an opportunity of personal hearing before the Enquiry Officer on 18.9.2002. After considering the reply of the said broker and oral submissions, the enquiry officer submitted his report to SEBI on 27.06.2003. He found that the said broker was guilty of violating Clause A(2) of Code of Conduct prescribed for Brokers and Regulation 4(b) of the FUTP Regulations. He recommended that the certificate of registration granted to the said broker may be suspended for a period of two months.

3.0 Subsequently a Show Cause Notice dated 02.07.03 was issued to the said broker calling upon him to show cause as to why the penalty recommended by the enquiry officer should not be imposed on him.

3.1 The said broker submitted his reply to the show cause notice vide letter dated 15.07.03. In his reply, the said broker submitted as under :- 3.1.1 Vide his letter dated 19.09.2001, he had informed the membership department of NSE that he had voluntarily suspended trading with effect of 19.09.01 and that since then his terminal had been deactivated.

3.1.2 Vide his letter dated 04.10.2001, he made an application to NSE for surrender of Trading membership with a request that the certificate of registration may be cancelled from 19.09.2001.

3.1.3 He had not committed any irregularity in respect of dealings in the scrip of MHL.

3.2 The said broker was granted an opportunity to be heard in person before the Whole Time Member, SEBI on 21.08.03 and in the course of hearing the said broker submitted that his reply to the show cause notice issued by Enquiry Officer might be treated as his reply to the said show cause notice and that he had no further submissions to make.

3.3 In view of the above, I am satisfied that the said broker has been granted sufficient opportunity to make his submission and that the requirement of natural justice has been met. Therefore, I proceed further in the matter.

4.0 I have considered the facts of the case, report of the enquiry officer, reply of the said broker and his oral submissions during hearing. The following issues arise for consideration: 4.1 Whether the said broker aided and abetted the creation of an artificial market in the shares of MHL and thereby violated Regulation 4(b) of the FUTP Regulations? 4.1.1 I note that there was a major spurt in the total volume in the scrip of MHL during the period August - November, 2000. From 29, 400 shares during January 2000 including nil volume for the entire month of July 2000, the trading volume increased up to 11, 34, 200 shares during the period August to November 2000. This is undisputed.

From the above, I note that the trading in the shares of MHL were very illiquid before the period under investigation and the volumes started going up from

August 2000 and were in the range of 20, 000 to 25, 000 shares per day till December 2000. Thereafter, the volumes in the scrip started declining and after January 15, 2001 the volumes came down to around 5, 000 shares per day. The volume spurt was observed mainly during the five month period viz. August to December 2000. I note that during the period between August 1999 - July 2000 (one year) the total volume traded at BSE was just 74, 700 shares, and whereas during the period between August 2000 to December 2000, it was approx. 19 lakh on the exchange.

4.1.3 I note that the price of the scrip at BSE, which was Rs. 193.30 as on August 25, 2000 rose to Rs. 264. 45 on September 09, 2000 and thereafter the price fell to Rs. 138.95 on November 27, 2000. The price on December 29, 2000 was Rs. 177.10.

4.1.4 I further found that at NSE, the volumes in the scrip during Middle of May 2000 to August 2000 were in the range of 200 to 500 shares and the scrip was infrequently traded. However, after August 25, 2000, the volumes in the scrip at NSE went up manifold and were in the range of 18, 000 to 25, 000 shares per day. For the period August 2000 to December 2000, the average trading volume at NSE was approx. 22, 000 shares per day.

4.1.5 I further note that the rise in price of the scrip of MHL was not justified based on the fundamentals of the company.

4.1.6 Therefore, I find that the scrip was essentially illiquid and that a false market had been created in the scrip in order to give an appearance of trading.

4.1.7 I further note that 80% of the total quantity of shares traded during the period June 2000 - December 2000 was between a few brokers of both BSE and NSE. In this regard, from the records of the trading details collected from the brokers of NSE & BSE I note that some of the clients of the broker were trading in the scrip through members of both BSE and NSE. They had enrolled as client to both BSE and NSE members and traded simultaneously in the scrip of MHL during the investigation period. I also note from the records obtained from different brokers of both the exchanges that most of these clients had not paid any margin to the brokers for the trades executed by them. Further, they were squaring off their positions not only at the end of settlement but almost on the same day. In this connection, I note that the brokers of both BSE and NSE confirmed to the investigating team that they had not carried out arbitrage business in the scrip during the period under investigation.

4.1.8 I note that the said broker has traded in the scrip of MHL mainly on behalf of M/s K P Investments and for Prashant Investment.

The details of the trading on behalf of M/s KP Investment are as under: The said broker has sold 12, 000 shares of MHL for Prashant Investment in settlement No. 37 of NSE. 4.1.9 In this regard I note from the records submitted by the said broker before the Enquiry Officer that no initial margin was collected from the client. The same was confirmed by the said broker in his sworn statement. He however added that the client used to square off his positions on the same day and therefore they did not collect any daily margin as well. On being queried by the Investigating officers as to why he allowed his client to trade in the scrip, especially when the stock which was not only illiquid but also trading at very high P/E, the said broker stated that the client normally used to square off his position on the same day.

Therefore, he believed that the client was doing jobbing in the scrip. Further, he had not allowed the client to take/give deliveries in the scrip. He also informed the investigating team that he was not aware about the dealings of the client with other brokers of the exchange.

4.1.10 In his reply dated 21.08.2002 to the show cause notice issued by the Enquiry Officer : - 4.1.10.1 The said broker has stated that one Mr. Janak Raja residing at Section IV, C-3/303 Shakti Nagar, Mira Road, Dist Thane 401107 known to him and who was his acquaintance /family friend, had introduced to me to Mr. Kisan Parwad, Proprietor of M/s . K P Investment and Mr. Prashant A Shah Proprietor of M/s . Prashant Investments.

4.1.10.2 The said broker has stated that he had paid commission to Mr. Janak Raja on the brokerage earned on the transactions of M/s .

K P Investment and M/s Prashant Investments 4.1.10.3 The said broker has stated that on behalf of M/s . Prashant Investments they had purchased 12000 shares of Morepen Hotels Ltd and had sold 12000 shares of MHL during settlement No. 37 covering period from 6th September to 11th September 2000 thereafter they had no transactions with the said M/s . Prashant Investments.

4.1.10.4 The said broker has stated that on behalf of M/s K P Investment they had effected transactions between 13th Sept. to 5thJanuary, 2001. The said M/s K P Investment used to square off the transactions on same day and the transactions were more or less in the nature of jobbing transactions. As the transactions were squared off at the end of the day they did not require margin deposit from the said constituents.

4.1.10.5 The said broker has stated that on an average the said constituents were purchasing and selling 500 - 1000 shares of MHL at once and at the end of the day their transactions stood closed out.

They did not find any risk in the said transactions and therefore they allowed M/s . K P Investment to carry their business through them.

4.1.10.6 The said broker has stated that the transactions were effected at the rate prevailing in the market. The transactions are of the nature of jobbing. There was no occasion for them to doubt the genuineness of the said transactions or bonafides of the constituents more so when the constituents were punctual in honouring their pay in obligation and had never defaulted.

4.1.10.7 The said broker has stated that they were not aware of any link between said M/s . Prashant Investments and M/s . K P Investment with M/s .Jem Fiscal Ltd or M/s . Hakeem Auto Ltd and for the first time in the enquiry report the said facts have been brought to our notice. They were also not aware that the said constituents have also effected transactions in the same scrip through any other member broker 4.1.11 The said broker has stated that te clients have entered into continuous speculative transactions in big quantities without any genuine interest in giving or taking delivery of shares. I also note that these clients were connected with each other and indulging in circular trading.

4.1.12 I further note that the said broker traded on behalf of the client over number of settlements which resulted in building up of artificial volumes and price in the scrip of MHL. It is finally the suspected innocent investors who would be trapped by such false appearance of trading in securities. This is detrimental to the interest of investors and the orderly development of the securities market.

4.1.13 In view of the above, I find that the said broker has aided and abetted his clients in creating a false and misleading appearance of trading by creating a false market with the scrip of MHL.

4.1.14 I note that Regulation 4(b) of the FUTP Regulations provides that: b) indulge in any act, which is calculated to create a false or misleading appearance of trading on the securities market.

4.1.15 In view of the above, I find that the said broker has violated Regulation 4 (b) of the SEBI(Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995 Regulations.

4.2 Whether the said broker has failed to exercise due diligence and exercise proper care in his dealing in the scrip of MHL and thereby violated Clause A (2) of the Code of Conduct for Stock Brokers provided in Schedule II to the Broker Regulations and thereby violated Regulation 7 of the Broker Regulations? 4.2.1 I note that, in the course of hearing before the Enquiry Officer the representative of the said broker submitted that as most of the time the transactions were squared off, by the end of the day no margin was payable and that the moment it came to the knowledge of the said broker that some enquiry has been initiated in the scrip by the authorities through the letter of the stock exchange, the said broker immediately stopped dealing with the clients and informed the exchange about the same 4.2.2 I agree with the finding of the Enquiry Officer that the submissions of the said broker are not convincing. The clients of the said broker traded only in the scrip of MHL which is illiquid.

These clients were new to the said broker and he permitted such clients to trade in essentially illiquid scrip and that too even without collecting margins Squaring of trades by the client is not an excuse not to collect margins.

4.2.3 I further note that despite the client entering into continuous speculative transactions, the said broker continued to trade for him. Any prudent stock broker would doubt the intention of his clients and stop trading for them in such circumstances. The said broker has not done so.

4.2.4 In this regard, I note that Regulation 7 of the Broker Regulations provides that - "7. The stock broker holding a certificate shall at all times abide by the Code of Conduct as specified in Schedule II".

4.2.6 I note that the Code of Conduct for Stock Brokers mentioned in Schedule II of the Broker Regulations provides that - (2) Exercise of due skill and care: A stock broker shall act with due skill, care and diligence in the conduct of his business.

It is borne out by the facts stated that the said broker did not exercise due skill, care and diligence while dealing with his said clients and as such I find that the said broker has not observed Clause A (2) of the Code of Conduct for the Stock Brokers and thereby violated Regulation 7 of the Broker Regulations.

5.0 I note that the Enquiry Officer, who was appointed in terms of Regulation 28(1) of the Un-amended Broker Regulations on 18.02.2002, has submitted his report to SEBI on 27.06.03 in terms of Regulations 13(1) of the "Enquiry Regulations" since the Broker Regulations were amended by the SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as "Enquiry Regulations") w.e.f 27.09.2002. I further note that the penalty in this regard is to be imposed under Regulation 13 of the Enquiry Regulations.

5.1 Therefore, in exercise of powers conferred on me under Section 19 of the SEBI Act read with Regulation 13 (4) of the Enquiry Regulations, I hereby suspend the Certificate of Registration bearing No.INB230649317 granted to Manoj J. Doshi for a period of 2 months. This order shall come into effect after 21 days from date of the order.