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N Vs. Brokerage P. Ltd.

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

Decided On : Jun-27-2006

Judge : N Sodhi, C Bhattacharya, R Bhardwaj

Appellant : N

Respondent : Brokerage P. Ltd.

Judgement :
1. The appellant before us is a registered stock broker on the Bombay Stock Exchange. The price of the scrip of Vision Technology India Ltd., (for short the Company) had shown a steep rise from Rs.4/- to Rs.14/- and thereafter to Rs.650/- whereafter there was a steep fall. The Securities and Exchange Board of India (for short the Board) conducted an investigation into the trading of the scrip of the company. It transpired during the course of the investigations that M/s. Harsha Pranav Securities Pvt. Ltd., and Vevenasri Financial Securities Pvt.

Ltd. were the two predominant traders in the scrip and that they traded through some brokers including the appellant herein. The investigations also revealed that these two traders had manipulated the price of the scrip. On receipt of the report from the investigating officer the appellant was issued a notice calling upon it to show cause why action be not taken for manipulating the scrip of the company in concert with the aforesaid two clients on whose behalf it had traded. It was also alleged that the appellant as a broker had not exercised due diligence in as much as it did not verify the financial antecedents of the clients before it allowed them to

place large orders while trading in the scrip of the company. An enquiry officer was appointed who after issuing a show cause notice to the appellant and on a consideration of the material collected by him came to the conclusion that there was no material on the record to show that the appellant as a broker had acted in concert with its clients or was in any way responsible for manipulating the price of the scrip of the company. The enquiry officer however, found the other charge established. He recorded a finding that the appellant had not exercised due diligence in as much as it allowed the clients to place large orders in the scrip of the company without verifying their financial background. On receipt of the enquiry report the Board issued another show cause notice to the appellant and a copy of the enquiry report was also sent. The appellant stoutly refuted the allegations made in the show cause notice and pleaded that it had not violated any code of conduct nor was it ever wanting in due diligence.

On a consideration of the enquiry report and the reply furnished by the appellant and after taking into consideration the material on the record including the statement of the representative of the appellant recorded during the course of the investigations, the Board accepted the recommendations of the enquiry officer and found that the appellant was lacking in due diligence in as much as it allowed large orders in the scrip of the company to be placed by the clients without verifying their financial antecedents. Accordingly, a minor penalty of suspension of the certificate of registration for a period of 15 days was imposed by order dated January 25, 2006. It is against this order that the present appeal has been filed under section 15T of the Securities and Exchange Board of India Act, 1992 (for short the Act).

2. We have heard the learned Counsel for the parties. It is clear from the record that the first charge leveled against the appellant regarding manipulation in the price of the scrip of the company in concert with its clients has not been established. As regards the second charge, it has been found that the appellant by allowing huge orders to be placed in the scrip of the company had aided and abetted the clients in creating an artificial market in the scrip. The appellant is a broker and in that capacity it would welcome orders for trading in the scrips of different companies because that is its business and this is precisely what it did. It is not the case of the Board that the appellant did not collect margins at the time of

executing huge orders for its clients. It is also not in dispute that there was never a default committed in complying with the market obligations. We cannot, therefore, uphold the finding recorded by the Board that the appellant by allowing its clients to place big orders without verifying their financial antecedents had not exercised due diligence required of a broker. When the representative of the appellant appeared before the investigating officer he categorically stated that the two clients on whose behalf the appellant had traded had been introduced by Mr. G. S. Sridhar who was the internal auditor of Krebs Biotech. This statement was not refuted and, therefore, the finding recorded by the Board is without any basis. The learned Counsel appearing for the Board tried to justify the impugned order on the ground that the agreements executed by the appellant with the clients before undertaking the trades on their behalf were not complete and some of the columns therein were blank. He took us through those agreements to contend that there was lack of due diligence on the part of the appellant as a broker and this was violative of the code of conduct. He also pointed out that the introducing party mentioned in the agreement is different from the one referred to in the statement of the representative of the appellant. We are unable to accept the contention of the Board for the simple reason that it was never alleged that the appellant had not executed proper agreements with its clients.

If that was the charge, it should have formed part of the show cause notice so that the appellant could have offered its explanation. Now at this stage we cannot look at those documents to record a finding that there was lack of due diligence on the part of the appellant. As already observed, adequate margins were collected by the appellant before executing the trades and this, in our opinion, was enough to reduce the risk of default. In this view of the matter, we cannot uphold the impugned order.

3. In the result, the appeal is allowed and the impugned order dated January 25, 2006 set aside with no order as to costs.

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