In Re: Sun Infoways Ltd.

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

Decided On : Dec-06-2007

Judge : V Chopra

Appellant : In Re: Sun Infoways Ltd.

Judgement :

1.1 Sun Infoways Limited (hereinafter referred to as "SIL"), promoted by Shri Shrikant Vasant Joglekar and Shri Sujit Shrikant Joglekar, was incorporated on June 29, 1994 as Best Mulyankan Consultants Pvt. Ltd. The main object of the company was to render consultancy services for valuation of assets such as land, building, machinery, agricultural land etc. This company was subsequently converted into public company on June 21, 1995. The name Sun Infoways Ltd. was adopted by the company after it changed its name with effect from May 11, 2000.

1.2 The company was listed on Bombay Stock Exchange Ltd (BSE) on May 16, 1996, after the public issue. Shri Joglekar and his family members sold their stake in SIL in the year 2000 to Shri Anil Pujari, Shri Rajan Tawate, Shri Tanvir Zaki, Shri Pravin Sonalkar, Ms Hafeza Vohra and Shri Kuldeep Handoo. Shri Manish Marwah introduced these persons to the old promoters. Shri Hemant Damodar Mehta, a consultant, introduced Shri Manish Kumar Marwah to Shri Joglekar and his family members.

1.3 It was observed that there was sudden spurt in price and volumes in the scrip of SIL at BSE in between February 2000 and December 2000. On February 9, 2000, only one trade for 100 shares was executed in the SIL scrip at a price of Rs. 10/per share for Rs. 1000/-. However, thereafter the price of the SIL scrip, continued to rise and reached a highest level of Rs 697/-on September 11, 2000 with volume going upto 24,800 shares.

1.4 SEBI initiated investigations into the alleged price manipulation in the trading of SIL shares between February 2000 and December 2000 (hereinafter referred to as "investigation period"). On analyzing the price/volume data of the SIL scrip during the investigation period, it was observed that rise in price of SIL scrip was accompanied with increased trading volumes allegedly effected through large number of entities, associated with the new promoters, directors and associates of SIL as well as few brokers including the broker IKM Investment Sevices Ltd with SEBI Registration No. BSE - INB 010794437766, CSE - INB 03079433986, NSE - INB 23079443807944, DSE - INB 050794435172 (hereinafter referred to as 'Noticee').

1.5 In the light of above facts, the trading details of the various entities who had traded in SIL scrip were collected and analyzed along with the data of the volumes contributed by these entities. It was observed that the transactions of the Noticee in SIL scrip during the investigation period contributed to the creation of some trading activity in the said scrip and also influenced the price of the scrip.

2.1 After considering the Investigation Report, SEBI appointed an Enquiry Officer to enquire into the violations allegedly committed by the Noticee under SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995, (hereinafter referred to in short as "PFUTP Regulations") and SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992 (hereinafter referred to in short as "Stock brokers Regulations") and bye laws, rules and regulations of the exchange.

2.2 A show cause notice dated December 20, 2004 was issued to the Noticee under Regulation 6(1) of SEBI (Procedure for holding Enquiry by Enquiry Officer and imposing penalty) Regulations, 2002 (hereinafter referred to as "the Enquiry

Regulations") to show cause, as to why enquiry proceedings should not be initiated against them for the violations of Regulation 4(a) and (b) of PFUTP Regulations 1995 and code of conduct as per schedule II read with Regulation 7 of Stock brokers Regulations.

2.3 The Noticee vide letter dated January 07, 2005 sought copies of additional documents which were provided by SEBI vide letter dated January 27, 2005. The Noticee vide letter dated March 15, 2005, submitted a detailed reply to the said show cause notice and also requested for a personal hearing before the Enquiry Officer. The opportunities of personal hearing given on January 30, 2006 and March 07, 2006 were adjourned to March 24, 2006 at the request of the Noticees. On March 24, 2006, Shri Pramod Jain, and Shri Rahul Malik, directors of the Noticee attended the hearing. Vide letter dated March 31, 2006, the broker furnished the copies of client registration forms of A.K Choudary, S.K Marwah, Rajender Rai and Ramesh Kumar.

2.4 The Enquiry Officer, after conducting enquiry in accordance with the provisions of the Enquiry Regulations submitted a report dated April 13, 2006. The Enquiry Officer in her report recommended a penalty of suspension of registration of the Noticee for a period of one month for their failure to exercise due skill, care and diligence.

3.1 Pursuant to the receipt of the Enquiry Report, Show Cause Notice dated April 26, 2006 was issued to the Noticee along with copy of the Enquiry Report advising them to show cause as to why the action, as recommended by the Enquiry Officer should not be imposed on them.

4.1 Noticee submitted its reply vide letter dated June 21, 2006 wherein they inter alia submitted as under: 4.1.1 That they were unaware of the manipulation in the price of SIL scrip.

4.1.2 That all the trades in question were executed by their sub-broker, CompuAction Securities Pvt. Ltd. and that there is no link or connection apart from the capacity as a stock broker and sub-broker.

4.1.3 That the trades were executed through the screen based trading system of the exchange where it was impossible to know the identity of counterparties.

4.1.4 That the trading pattern of their sub-broker CompuAction did not give any suspicion as would have alerted them as to any irregularity.

4.1.5 That they are not responsible for the wrong doing of the clients and that in the year 2000 it was very difficult to monitor the trades of the sub-broker and their clients and now they have installed surveillance system and are periodically reviewing the trading of their clients.

4.1.6 That the enquiry officer does not have any categorical finding that they were directly involved in the alleged manipulation and that they have not violated any of the provisions of PFUTP Regulations.

4.1.7 That the suspension of their registration for a single day would amount to a commercial death.

4.1.8 That they were in the business of stock broking for a period of about 11 years and never faced any proceedings like this.

4.1.9 That their turnover during the period February 2000 to December 2000 was for Rs 5,524 crores whereas for the same period the turnover in SIL scrip for all the clients and sub-brokers was 35 crores i.e. 0.64% of their turnover on BSE.
4.1.10 That the rise in price and increased volume can not be considered as the factor for manipulation.

4.1.11 That there was no proprietary trades in SIL scrip and they did not gain any benefit except for brokerage income earned from the normal course of business.

4.1.12 That the list of clients mentioned in the enquiry report is incomplete since they did not trade on behalf of Laxmi Capital and K M Agrawal and further the 13 other clients who had traded in the scrip through them during the investigation period were not mentioned in the enquiry report.

4.1.13 That Shri Pramod Jain had only mentioned that their sub-broker CompuAction had executed trades through the terminal located at CompuAction's premises.

4.1.14 That Shri Pramod Jain did not state that he did not know when CompuAction started trading with them instead he stated that he was unaware about the date and in fact informed the enquiry officer of the date of starting the trade. He did not state that Shri Subhash C Sahni was a director of IKM, but he is a director of CompuAction.

4.1.15 That they denied the execution of trades by CompuAction for their client Ashok Chaudhary at NSE through them and also denied that Shri Ashok Chaudhary was their direct client.

4.1.16 That they have also denied that Shri Pramod Jain confirmed that Sudesh Kumar Marwah was introduced by Ashok Chaudhary to CompuAction and also denied that Shri Pramod Jain confirmed that Ramesh Kumar was introduced by Ashok Chaudhary to CompuAction.

4.1.17 That Shri Rajendra Rai was not introduced by Shri Dilip Nabera and as per KYC obtained from CompuAction he was a "walk in client" and was not introduced by a third person at all.

4.1.18 That they were unaware about the matching transactions of the sub-broker's client and they had no relationship with the clients on whose behalf the transactions were executed.

4.1.19 That they have done broking business for CompuAction for almost 250 scrips and not just in SIL.

4.1.20 That CompuAction had been registered as a sub-broker on BSE w.e.f. Marcy 16, 2000 and at the relevant time, the broker was not required to maintain accounts of clients of sub-brokers and maintained only the accounts of the sub-broker as part of his client ledger.

4.1.21 That they have not violated any of the provisions of PFUTP Regulations and Stock Brokers Regulations.

5.1 An opportunity of personal hearing was given to the Noticee before me at SEBI's Head office at Mumbai on July, 20 2007. Shri Rahul Malik and Shri Pramod Jain directors of the Noticee accompanied with their Advocates Shri Somasekhar Sundaresan, Shri Joby Mathew and Ms. Deepika Vijay, Advocate attended the hearing. They have also filed written submissions vide letter dated August 17, 2001. The main contentions raised by them are given hereunder: 5.1.1 The Noticee stated that they have been in the business of stock broking for more than 45 years and employed over 200 persons and during the investigation period, they had a wide network of 152 SEBI registered sub-brokers as also having 312 trading terminals and were dealing in 300 -350 scrips per day.

5.1.2 They have also stated that there were no proprietary trades in SIL as also there was no trading for their direct clients (except sale of 200 shares by one client, Ms Sumati).

5.1.3 The practice prevalent in the year 2000 was that the broker and sub-broker would enter into an agreement and that the sub-broker in turn would enter agreement with their clients. The entire process of registration of clients including KYC details was the responsibility of the sub-broker. The Noticee did not issue contract notes to clients directly, instead a consolidated contract note were issued to the sub-broker who in turn issued confirmation memos to their clients. They alleged that the Enquiry Officer had applied the current regulations of Tripartite Agreement to be executed by Broker, Sub-broker and client jointly which were in effect from April 01, 2005. They also stated that the broker was not required to maintain the client ledger contrary to as alleged by the Enquiry Officer.

5.1.4 The Noticee alleged that the Enquiry Officer has made a statement in her report that IKM did not know when CompuAction started trading with them which according to them is wrong. They stated that their director had only stated that the same would be provided shortly.

5.1.5 The Noticee alleged that the Enquiry Officer wrongly mentioned that Subhash Sahni was a common director of IKM with CompuAction where as in fact Pramod Jain had stated that Subhash Sahni was a common director of CompuAction Securities with the NSE broker CompuAction Financial Services Pvt.

Ltd. 5.1.6 The Noticee denied that Pramod Jain had even made a statement that Sudesh Kumar Marwah was introduced to CompuAction by Ashok Kumar Chaudhary.

5.1.7 The Noticee stated that Pramod Jain never confirmed that Ramesh Kumar was introduced to CompuAction by Ashok Kumar Chaudhary.

5.1.8 The Noticee submitted that neither the sub-broker CompuAction nor its client Ashok Kumar Chaudhary had traded through them on NSE. 5.1.9 The Noticee submitted that Ashok Kumar Chaudhary was not their client, instead he is a client of CompuAction.

5.1.10 The Noticee has given certain instances such as change in the business of SIL, acquisition of US based E-commerce company, revenue escalation etc. as reasons for the rise in price and volume of SIL scrip.

5.1.11 CompuAction Securities was a registered sub-broker of the Noticee on BSE vide SEBI registration No. INS010579238 dated March 16, 2000 based on an application dated January 17, 2000 whereas the investigation period in the scrip of SIL commenced from February 2000. All the relevant copies of the application form, agreement and SEBI certificate were handed over to enquiry officer at the time of personal hearing. The enquiry officer has wrongly quoted DSE sub-broker registration No. and date in the enquiry report instead of relevant registration of BSE as stated above.

5.1.12 The Noticee reiterated their unawareness of the counterparties, matching transactions of the clients of the sub-broker.

5.1.13 The Noticee submitted that they have not violated the provisions of PFUTP Regulations and Stock Brokers Regulations and requested for further hearing in the matter.

6.1 After examining findings of investigation, enquiry report, show cause notice and reply of the Noticee, I find that the matter can be decided on its merit and a further hearing as requested by the Noticee in their written submission is not warranted.

6.2 I observe that consequent to a change in shareholding of SIL during January 2000, large scale volumes were witnessed in the trading of the SIL scrip. The price of SIL scrip had shot up from a low of Rs 10 as on February 9, 2000 to Rs 697/- on September 11, 2000.

6.3 It is further observed that the trades in SIL shares were executed by certain connected entities as well as a few sub brokers and brokers, who indulged in artificial trades resulting in the manipulation of SIL scrip. The Noticee was one of the top buyer and seller broker who had a gross buy position of 4,26,958 shares and a gross sale position of 4,36,399 shares representing 14.19% and 14.50 % of the total volume at the exchange in SIL scrip. However, it is seen that sub-brokers were doing most of these trades. The Noticee submitted that their sub-broker, CompuAction had executed trades in SIL for their clients through them and Noticee had never transacted in the scrip of SIL on their own account. The Noticee had dealt for only one direct client (Ms. Sumati) who had sold 200 shares during the investigation period.

6.4 The Enquiry Officer had referred some of the statements of Shri Pramod Jain, which according to the Noticee, was misinterpretation of statement to prove the nexus between the Noticee and their sub-broker CompuAction and their clients. On examination of his original statement, I find that the above stand of the Noticee is correct. Shri Pramod Jain had not stated that he did not know when CompuAction started trading with them; instead he stated that he was unaware about the date and in fact informed the enquiry officer of the date of starting the trade. He had also mentioned that their sub-broker CompuAction had executed trades through the terminal located at CompuAction's premises.

6.5 I have noted Shri Pramod Jain did not state that Shri Subhash C Sahni was a director of the Noticee. In fact, he had stated that Subhash Sahni was a common director of CompuAction Securities and the NSE broker CompuAction Financial Services Pvt. Ltd. He never confirmed that Sudesh Kumar Marwah was introduced by Ashok Chaudhary to CompuAction or Ramesh Kumar was introduced by Ashok Chaudhary to CompuAction. The Noticee submitted that Ashok Kumar Chaudhary was not their direct client; instead he was a client of CompuAction, their sub-broker. Hence, the nexus between the Noticee and their sub-broker CompuAction suggested by the Enquiry Officer was contrary to facts. In view of this, the Noticee should be given the benefit of doubt as regards their alleged role in the manipulation in SIL. Further, viewed from the relevant legal position, I feel that there is no sustainable evidence on record to prove the charges levelled against them under the provisions of PFUTP Regulations in the show cause notice.

6.6 The next issue is whether the Noticee had violated the provisions of Code of Conduct as per the Stock Brokers Regulations.

6.7 I have examined the pattern of trading of the sub-broker through the Noticee and find that they bought 36000 SIL shares for Rajendra Rai from Rajesh Kumar Choudhary whose broker was N.C Jain. At the same time, Rajesh Kumar Choudhary bought 43100 SIL shares from Rajendra Rai through sub-broker, CompuAction Securities. Their trades were approximately 1.5% of the total trades in SIL scrip during the investigation period. I find that they have consistently executed trades and also reversed their transactions on the same day i.e. buying and selling on both sides for the same clients for almost the same number of shares. The instances of such reversal in position of the trades are given hereunder: 6.8 From the above table, it is clear that Rajendra Rai and Rajesh Chaudhary were buying and selling the shares at the same time, through the brokers i.e. the Noticee (through its sub-broker) and N C Jain. The trades as shown in the table above merely reflects the reversal of positions without the actual change in beneficial ownership, in as much as on many days, the same number of shares were bought and sold i.e.

positions were merely reversed on the same day by these two clients while trading through these two brokers in just one scrip i.e. SIL.

When client of the sub-broker of the Noticee was buying, N C Jain was selling and vice versa. These transactions were spread across July to November 2000 and were well within the period of investigation and clearly gave a misleading appearance of trading. Further, these transactions also resulted in the creation of an artificial market and volumes and thereby enhancing liquidity in the otherwise illiquid scrip of SIL.

6.9 Apart from the above transactions, Shri Ashok Kumar Chaudhary bought 1200, SIL shares through the Noticee from Rajesh Kumar Chaudhary, brother of Ashok Chaudhary through N C Jain. Further, Ashok Kumar Chaudhary sold 9500 and 800 shares to Rajendra Rai and Rajesh Kumar Chaudhary. Ashok Kumar Chaudhary and Rajender Rai, through the Noticee sold 3000 shares to R. S. Investment for Telefinlease (a company belonging to S. K. Marwah, Suman Pandit and Anil Raina). Ashok Kumar Chaudhry bought 1200 shares from Apoorv through Shilpa Stock Brokers.

6.10 The Noticee for the clients of its sub-broker and the counter party broker JCL Securities Pvt. Ltd. had traded the total volume of 32,600 shares out of which 19200 shares were matched, which represented 59% of the total trades between them for their respective clients. An analysis of the table given above shows that 89 of the trades between the Noticee (for its sub-broker's clients) and JCL were found to be structured and were executed on 18 trading days and several client codes were indisputably used for AFPL viz. 4131,4015,3001,9A03,ADH, ADHUNIK, ADHU, ADUNIK and 4024.

6.11 The Enquiry Officer had given the full details of transactions executed by the sub-broker through the Noticee. From the trade details, it is established that there were numerous instances of transactions executed through the Noticee, with the same counter party, in only one scrip, wherein the buy and the sell orders were placed at almost the same time, between the two entities, with a time difference of placing orders in less than a minute. This proximity in the putting of orders at the same price and for the same quantity, resulted in the trades getting matched, in all the three parameters i.e. quantity, price and most importantly, the time, required to conclude the trades to the extent of two decimal places. All these factors to very large extent, indicated synchronization in the logging in of the orders, albeit executed on the screen of the exchange. However, the Noticee has submitted that their sub-broker CompuAction had executed trades through them. In this regard, I note that their sub-broker CompuAction was not a registered sub-broker at the relevant time. However, the Noticee submitted in their written submission that the sub-broker's flagship affiliate company namely CompuAction Financial Services (P) Ltd was a member of NSE since 1996 i.e much prior to the investigation period.

Admittedly, the registration of CompuAction as a sub-broker of the Noticee at BSE was granted on March 16, 2000. The investigation period in SIL scrip stated from February 2000. It is seen that the reversal trades in question were carried out after CompuAction became a registered sub-broker. However, the other trades executed by the sub broker through the Noticee prior to its registration do not validate retroactively because of subsequent application to SEBI for registration. The onus to check as to whether the sub broker is registered with SEBI lies upon the main broker. This has been clearly brought out in the SEBI Circular No. SMD/Policy/Circular/3-97 dated March 31, 1997 and has evidently not been complied with by the Noticee.

Further, Noticee is responsible for the wrongdoing of an unregistered sub-broker as the Noticee had facilitated their sub broker to execute large number of matched trades which created false market in the scrip.

Further, even if the sub-broker is registered, a stock broker can not shy away from the responsibility of ensuring the authenticity of the trades executed through its terminal.

6.12 The Noticee should have exercised due care and diligence as also should have verified whether an entity is registered or not. In the instant case, Noticee allowed CompuAction to execute number of trades prior to get their registration as sub-broker. The Noticee is responsible to verify the trades executed by the sub-broker even though the trades were on the BOLT system of the BSE. The terminal installed in the office of CompuAction is not a ground to defend since the Noticee can access the said BOLT terminal online and could have verified the gross sell and buy positions of their sub-broker as they were the largest buyer and seller in the scrip. Further, the Noticee should have taken suitable measures to check any apparent irregularity noted in the deals executed through them, irrespective of the trades executed on the screen of the exchange. In fact, the Noticee had suspended the business of the said sub broker vide their letter dated 19-2-2005. The Noticee should be fully responsible for the acts of the sub-broker and their clients when they fail to exercise necessary due diligence essentially required in conducting the business of a stock broker. The Noticee has thus violated Regulation 7 read with the Clause A(2) of Code of Conduct as specified in Schedule II of Stock Brokers Regulations, which provides that A (2) EXERCISE OF DUE SKILL AND CARE: A stock-broker, shall act with due skill, care and diligence in the conduct of all his business.

6.13 However, at the same time, in the absence of any evidence linking the Noticee, its sub-broker and the ultimate clients, as also since the charges levelled under the provisions of PFUTP Regulation are not established against the Noticee, I am of the view that a minor penalty of 'censure' against the Noticee is sufficient for the violation of code conduct as stated in paragraph No. 6.12 above.

7.1 Therefore, in exercise of the powers conferred upon me in terms of Section 19 of the SEBI Act, 1992 read with Regulation 13(4) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002, I hereby impose a minor penalty of 'censure' to the broker IKM Investment Services Ltd. (SEBI registration No. BSE - INB 010794437766, CSE - INB 03079433986, NSE - INB 23079443807944, DSE - INB 050794435172 and PAN No. AAACI2174G).