BEFORE THE SECURITIES APPELLATE TRIBUNAL MUMBAI

Appeal No. 76 of 2012

Date of Decision : 11.05.2012

H.J. Securities Pvt. Ltd.
24/26, Cama Building,
Dalal Street, Fort,
Mumbai – 400 001. …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. J.J. Bhatt, Advocate with Mr. Pratham Masurekar, Advocate for the Appellant.

Mr. Kumar Desai, Advocate with Mr. Mihir Mody and Mr. Mobin Shaikh, Advocates for the Respondent.

CORAM : P.K. Malhotra, Member & Presiding Officer (*Offg.*)
S.S.N. Moorthy, Member

Per : P.K. Malhotra

This order will dispose of two Appeals no. 76 and 81 of 2012 which arise out of identical facts. The appeals were heard together and, with the consent of the parties, are being disposed of by a common order. For the sake of convenience, the facts are being taken from Appeal no. 76 of 2012.

2. The appellant company is a stock broker having its registered office at Mumbai. It is said to be doing proprietary trading from 2 locations through 19 terminals in Mumbai. The terminals are operated by ‘jobbers’ authorized by the appellant. It traded in the scrip of Edserv Softsystems Ltd. (the company) on the first day of its listing on March 2, 2009 and for a few days thereafter. Since price of the scrip saw an upward movement, the Bombay Stock Exchange Ltd. and the National

Stock Exchange of India Ltd. carried out investigations for the period from March 02 – 06, 2009 and March 02 – 09, 2009 respectively into the trading of the scrip. Subsequently, the Securities and Exchange Board of India (the Board) also carried out investigations and noted that the appellant and two other brokers traded in the scrip in their own account constituting about one-third of the total trades on the day of listing i.e. March 2, 2009. It was also noted by the Board that these three brokers executed self trades resulting in violation of Regulation 3 and 4 of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (FUTP regulations) and also violation of code of conduct for stock brokers as prescribed in Schedule II under Regulation 7 of the Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Regulations, 1992. The details of the trades executed by the three brokers which constitute approximately one-third of the total trades, as given in the show cause notice, are under:

Broker (Client)	Gross Purchase (GP)	GP as % of Traded Qty.	Avg. Purchase Rate	Gross Sale (GS)	GS as % of Traded Qty.	Avg. Sell Rate	Net buy/ (Sale)	No. of BUY trades with Q = 1 share	No. of SELL trades with Q = 1 shares
OPG (Own)	64,16,716	18.81	112.27	64,16,716	18.81	112.39	0	4523	2860
HJSL (Own)	28,33,872	8.31	110.56	28,33,872	8.31	110.62	0	2011	1206
MEPL (Own)	21,30,360	6.25	106.60	21,30,360	6.25	106.60	0	1607	868
Total	1,13,80,948	33.37		1,13,80,948	33.37		0		

The summary of the alleged fictitious trades, as executed by the appellant, is also given in the show cause notice as under:

Member (Client)	Date	Buy Qty.	Self Trades (No. of shares)	Self Trades as a % of total buy by client	Total traded Qty. in the scrip on the day	Self Trades as a % of total traded qty in the scrip on the day
HJSL (Own)	March 02, 2009	28,33,872	2,00,725	7.08%	3,41,04,135	0.59%
	March 03, 2009	2,68,183	23,036	8.59%	42,19,116	0.55%
	March 06, 2009	1,38,362	1,215	0.88%	36,13,192	0.03%

3. A show cause notice dated June 24, 2011 was issued to the appellant asking it to show cause as to why enquiry should not be held against it and penalty imposed for the aforesaid violations. The appellant submitted its reply dated July 18, 2011

denying the allegations and submitted that on March 2, 2009, when the scrip of the company was listed on the stock exchanges, 19 jobbers of the appellant traded on its behalf in the scrip of the company from different terminals at different locations and each jobber did transactions according to his own judgment in the course of his regular trading activity. There was no cross connection in putting the buy and sell orders. The jobbers placed orders from their terminal and they had no knowledge for orders placed by other jobbers at different terminals. In some cases, the buy order of the same quantity placed by one jobber matched at the same time with the sell order by another jobber and the order got executed through online trading process. There was no intention to execute fictitious trades. All the trades executed by the appellant were proprietary in nature and the appellant had no connection either with the promoters or directors of the company. The alleged fictitious self trades which matched on the day of listing are only to the extent of 0.59% of the total traded quantity on the day of listing which is an insignificant percentage keeping in view the total volume of trades and the fact that trades were being entered through 19 different terminals. The explanation offered by the appellant was not accepted by the Board and the adjudicating officer, by the impugned order, held the appellant guilty of violating Regulation 3(a), (d) and 4(1), 4(2) (a) and (g) of the FUTP regulations and code of conduct for stock brokers as prescribed in Schedule II of the stock broker regulations and imposed a penalty of ₹ 3,50,000 under section 15 HA and 15 HB of the Securities and Exchange Board of India Act, 1992 (the Act). Under similar circumstances, the appellant in Appeal no. 81 of 2012 also traded in the same scrip adopting the same modus operandi and a consolidated penalty of ₹ 1,50,000 has been imposed upon it. Hence these appeals.

4. We have heard Mr. J.J. Bhatt, learned counsel for the appellants and Mr. Kumar Desai, learned counsel for the respondent Board who have taken us through the records. The trades as mentioned in the show cause notice and executed by the appellant are not disputed. The only defence advanced by learned counsel for the appellant is that the impugned trades were carried out by 19 jobbers of the appellant in appellant's pro-account and such trading from different terminals is

permitted by the stock exchange. In support, learned counsel for the appellant placed on record extract from the inspection manual of the Bombay Stock Exchange containing instructions regarding pro-account trading. The said instructions, issued in 2003, inter alia, provide that in case any member-broker requires the facility of using own account through trading terminals from more than one location, such member-broker shall be required to submit an undertaking to the BSE stating the reason for using the own account at multiple locations and the Exchange may, on case to case basis after due diligence, consider extending the facility of allowing use of own account from more than one location. It is the case of the appellant that vide letter dated April 24, 2009 (copy placed on record), the appellant had furnished details of the terminals from where the appellant wished to avail of the facility of placing order on pro-account. It was, therefore, submitted by the learned counsel for the appellant that since he had placed orders in the scrip through his pro-account operating through jobbers through different terminals, the possibility of some of the trades getting matched is not ruled out and such percentage is only 0.59% of the total trades executed by the appellant which cannot be considered to be objectionable. There was no malafide intention on the part of the appellant in executing these trades and hence the appellant cannot be held guilty of violating the provisions of FUTP regulations or the code of conduct prescribed for the stock brokers.

5. On the other hand, learned counsel for the Board submitted that the facility given by the stock exchange of using own account through trading terminals from more than one location has been misused by the appellant by executing trades through jobbers who are independent day traders. Learned counsel for the respondent Board has also drawn our attention to the standard format of the agreement entered into by the appellant with various operators, who are referred to by the appellant as ‘jobbers’ and submitted that as per the agreement the relationship between the appellant and the operator is not one of employer-employee or that of broker, sub broker or that of a broker remisier / authorized person. It is in fact a system devised by the appellant by which he has permitted these operators to use its account for the purpose of sharing profit which does not fall within the scheme of pro-account trading. A similar

modality has been adopted by some other brokers too which has resulted in the manipulation of the scrip. If such a trading is allowed in pro-account through various terminals to the brokers, the possibility of a large number of self trades being executed and giving a wrong impression about the trading of the scrip in the market to lay investors is not ruled out. Such an arrangement cannot be permitted as it breaches the regulatory framework established by the Board.

6. We have considered the rival submissions and are inclined to agree with the view expressed by learned counsel for the Board. The modus-operandi of the appellant in operating through the 19 jobbers from different locations has resulted in fictitious trades / self trades where the buyer and the seller are the same party. Such trades create artificial volume in the traded scrip and send wrong signal to the lay investor with regard to trading in the scrip. The Board has come to a definite finding that the appellant had executed self trades on the day of listing for 2,00,725 shares which was 7.08% of its total quantity i.e. one in every fourteen trades of the appellant's total buy quantity on that day was a self trade on its proprietary account in terms of volume. Similar is the situation on the sale side. It is further noted by the Board that trading pattern in the subsequent day also reflects that one out of eleven trades of the appellants' total buy quantity was a self trade on its proprietary account in terms of volume. This finding of the Board is not disputed by the appellant. If the appellant was operating through jobbers from different terminals, he should have placed some mechanism in place to ensure that his trades do not result in self trades. Simply because the number of such self trades is not large by itself cannot justify execution of self trades. The appellant is free to adopt any business model but he has to ensure that whatever business model he adopts, it is in conformity with the regulatory framework. Since the business model adopted by the appellant has resulted in self trades which are considered to be fraudulent, we cannot find any fault with the impugned order which has held the appellant guilty of violating the provisions of FUTP regulations as well as code of conduct for the stock brokers. We are, therefore, not inclined to interfere in the matter.

7. It was then argued by learned counsel for the appellant that penalty imposed under section 15 HA and 15 HB of the Act is grossly unreasonable and it does not have any nexus with the purported gravity of the charge of fictitious / self trades in the scrip of the company. The appellant is a stock broker and he understands the implication of his actions well. Self trades, which implies the trades in which both buyer and seller are the same party and does not result in change of beneficial ownership are fictitious in nature and they create artificial volume in the scrip sending wrong signal to the lay investor about trading in the scrip. A person found to be guilty of violating FUTP regulations can be imposed a penalty of ₹ 25 crore or three times the amount of profit made, whichever is higher, under Section 15 HA of the Act. However, the Board has imposed a penalty of ₹ 3 lacs only. Similarly for violation of code of conduct for stock brokers, a penalty which may extend to ₹ 1 crore can be imposed under section 15 HB of the Act. However, the Board has imposed a penalty of ₹ 50,000 only. Similarly, in Appeal no. 81 of 2012, the Board has imposed a penalty of ₹ 1 lac and ₹ 50,000 under section 15 HA and 15 HB of the Act on the appellant. In the facts and circumstances of the case, we find the penalty imposed by the Board on the two appellants to be just and reasonable.

In the result, both the appeals fail and are dismissed with no order as to costs.

Sd/-
P.K. Malhotra
Member &
Presiding Officer (*Offg.*)

Sd/-
S.S.N. Moorthy
Member

11.05.2012
Prepared and compared by:
msb