BEFORE THE SECURITIES APPELLATE TRIBUNAL MUMBAI

Appeal No. 11 of 2013

Date of Hearing : 19.09.2014

Date of Decision : 14.10.2014

JHP Securities Pvt. Ltd.
201/B Dev Neo Vikram,
New Link Road,
Above Audi Car Showroom,
Andheri (West),
Mumbai – 400 053. …Appellant

Versus

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

Mr. V.M. Singh, Advocate for the Appellant.

Mr. Kumar Desai, Advocate with Mr. Mihir Mody, Advocate for the Respondent.

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

Per : A.S. Lamba

1. The present appeal has been filed by JHP Securities Pvt. Ltd. ("JHP" or "Appellant" for short) against Securities and Exchange Board of India ("SEBI" or "Respondent" for short), for imposing penalty of Rs.6,00,000/- under Section 15HA of Securities and Exchange Board of India Act, 1992 (SEBI Act for short) for violation of Regulations 4(1), 4(2)(a), 4(2)(e) of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003

(PFUTP Regulations for short) and Rs. 2,00,000/- under Section 15HB of SEBI Act for violation of Clauses A(1) to A(5) of Code of Conduct for Stock Brokers under Securities and Exchange Board of India (Stock-Brokers and Sub-Brokers) Regulations, 1992 (Stock-Brokers Regulations for short).

2. A Show Cause Notice (SCN) was issued to Appellant by Respondent vide its letter dated May 31, 2010; wherein findings of investigation, considered relevant for purpose of proceedings, and allegations were mentioned.

3. Facts of the case against Appellant, in brief, are as given below:-

- Promoters of Gemstone Investment Limited (GIL or company for short) reduced their shareholding in company, which was accompanied by unusual increase in price of companies scrip during IP (August 28, 2006 to August 21, 2008).

- Appellant, trading on behalf of its six clients during Investigation Period (IP) - who were part of larger group of entities herein called Narendra Ganatra Group (NG Group), - had highest concentration in purchase and sale in scrip of the company during IP.

- Entities of NG Group traded in scrip of GIL on BSE – under different client codes and also engaged in off-market deals in scrip of GIL, - price and volume of GIL scrip by entering into synchronized, circular and reversal trades.

- One of the NG Group entity was Devendra A Vadhaiya, who was also terminal operator and person-in-charge of branch office of Appellant located in Andheri; from which most of alleged synchronized, circular and reversal trades in GIL scrip, were executed.

- Narendra Ganatra was part of NG Group entity and was also Director of GIL and he was link between NG Group entities and GIL.

- On basis of analysis of trades of Appellant, on behalf of its six clients, in scrip of GIL and considering its substantial volume and synchronized, circular and reversal trades to manipulate price and traded volume, it was alleged by Respondent that Appellant violated regulation 4(1), 4(2)(a), 4(2)(e) of PFUTP Regulations and Clauses A(1), A(2), A(3), A(4) and A(5) of

Code of Conduct for Stock-Brokers as stipulated under Schedule II read with regulation 7 of Stock-Brokers Regulations.

4. In reply of SCN and in MOA, the following are the submission of Appellant:-

- Appellant is in business of stock broking since 1984 and has 70 employees.
- Appellant has not carried out any trade in GIL scrip in proprietary account and has no relation / connection with any of its clients named in SCN, except Stock-Broker and constituent relationship.
- All transactions carried out for its clients were through market mechanism where there is complete anonymity to counter party and all transactions were backed by delivery and all settlement obligations were duly met.
- Devendra Vadhaiya was terminal operator at relevant time and he ceased to be so in year 2008.
- Appellant has maintained highest standards of integrity and had always exercised due skill, care and diligence in its functioning.

5. From allegations, submissions of Appellant and material on record, it has been observed by Ld. AO that:-

- Appellant traded on behalf of its clients, namely, Prem Parekh, Mala Hemanth Seth, Kishore Chauhan, Hemanth Seth, Bhavesh P Pabari and Ankit Sanchaniya and purchased 71,62,146 shares of GIL (constituting 28.5% of total market volume) and sold 68,40,013 shares of GIL (constituting 26.78% of total market volume during IP).
- These six clients were related / connected with each other and with larger group, which included Devendra Vadhaiya – who was terminal operator from which alleged synchronized, circular and reversal trades were executed.
- Therefore, Appellant, acting in collusion with its clients and others indulged in synchronized, circular and reversal trades, in order to manipulate price and volume of GIL scrip.

6. From other observations of Ld. AO from impugned order it is seen that six clients of Appellant, namely, Prem Parekh, Mala Hemanth Seth, Kishore Chauhan, Hemanth Seth, Bhavesh P Pabari and Ankit Sanchaniya are related and connected to each other and are part of a larger group which has another 11 members, namely Bharat Thakker, Narendra Ganatra, Manish Joshi, Rajesh Bhanushali, Vinayak Bhanage, Bhupesh Rathod, Janak Vyas, Devendra A. Vadhaiya, Jayesh Kuwadia, Ashish Ganatra and Nimesh Ganatra and these 11 persons along with earlier named 6 persons from part of Narendra Ganatra Group (NG Group), who are related and connected to each other. Now these Narendra Ganatra Group 17 entities have connived with each other and with another 10 persons; namely Premchand K Shah, Sharman P Shah, Nihal P Shah, Sharman Appliances Pvt. Ltd., Mradula V Shah, Sushila P Shah, Vijay Kumar N Shah, Shreya V Shah, Bindi Shah, Vanechand Vora; who are Chairman and Managing Director, Director / Promoter, related to Director / Promoter (GIL Group), in such a manner that entities of NG Group were executing reversal / circular trades in GIL scrip and manipulating volume, as well as price, of GIL scrip, while entities of GIL group were selling their shareholding in GIL, in the market and through synchronization, majority of these sales by GIL group was finding its way to entities of NG Group.

7. For trades of Nihal P Shah, Sharman Appliances Pvt. Ltd. Sushila P Shah, Sharman P Shah and Premchand K Shah, counter parties were Manish Joshi, Bhavesh Pabari, Narendra Ganatra, Vinayak Bhanage, Hemant Sheth, Prem Parekh, Bharat Thakker, Mala Sheth and Kishore Chauhan. GIL Group and NG Group, consistently traded in GIL scrip from August 28, 2006 to August 21, 2008 (IP) and were instrumental in price rise of scrip

from Rs. 2.94 to Rs. 51.81 by placing buy orders at incremental prices and indulging in synchronized / circular / reversal trades.

8. Analysis of trade and log also reveals that trades of GIL Group, matched with NG Group. It was observed that during period from August 28, 2006 to March 16, 2007, out of 13,03,800 shares sold by GIL group, NG Group bought 9,45,500 shares (72.51%) and for 11,56,680 shares sold by GIL Group between March 20, 2007 to July 3, 2007, NG Group was counter party for 8,96,619 shares i.e. 77.5%.

9. It may also be mentioned that GIL Group owned 69.65% of paid up capital of GIL as on quarter ending June 30, 2006 which got reduced to 1.22% at end of quarter September 30, 2008, as a result of sale by promoters i.e. GIL Group.

10. Appellant has admitted that it had traded in scrip of GIL, on behalf of its six clients during IP. It is not in dispute that these six clients of Appellant had acted in collusion amongst each other and with other entities of NG Group in synchronized / circular / reversal manner and thereby artificially increased volume / price of GIL scrip. Appellant has however stated that its relationship with its clients is that of client-broker and it is not connected / related with any of its clients or other NG Group clients and that matching of such transaction between GIL Group and NG Group and amongst NG Group entities, is merely a coincidence, as trading was done in stock exchanges' anonymous trading system.

11. It is a matter of record that NG Group had purchased 1,15,49,999 shares in GIL scrip during IP in circular / reversal trades and also sold 1,15,49,999 shares in similar manner, which constituted majority (more than

50%) of total shares bought / sold during IP and Devendra Vadhaiya was part of such trading and it was Devendra Vadhaiya's terminal from where orders for buy/sell of six clients of Appellant originated.

12. Mr. V.M. Singh, Ld. Counsel for Appellant vehemently argued that it was Appellant's dealer, who was part of NG Group and was placing orders for trade in GIL scrip for six clients of Appellant and these trades may be manipulative in nature but there is no evidence to implicate Appellant, for deeds for his dealer for such manipulative trades.

13. Ld. Counsel for Appellant bought out case law for imputing vicarious liability to Appellant for acts / deeds of his employee. In this context Appeal Suit No. 10 of 2002 between N. Sridhar vs. Maruthi Jayaraman & Anr., decided by Hon'ble High Court at Madras was cited. In this case Jayaraman, an employee of M/s. M.R.F. Ltd., in course of employment, stole 350 shares lodged for transfer, prepared false transfer deed and presented shares for sale and realized Rs. 4,01,500/- as sale proceeds.

14. The trial court concluded that on appreciation of oral and documentary evidence, original share holder is entitled to claim suit amount from Jayaraman and not from his employer.

15. Dissatisfied with this judgment, original share holder preferred appeal before Hon'ble High Court and it was held that for master's liability to arise, act must be wrongful one, authorized by master or a wrongful one and unauthorized mode of doing some act, authorized by master. In instant case, omission and commissions pointing out to misdemeanor or malevolent conduct of employee and all these were of individual, independent and personnel, unauthorized wrongful acts of said employee and in view of the matter, the liability could not be tagged on to employer.

16. Working of Stock Exchanges and its Members (Stock-Brokers) is governed by Rules, bye-laws, regulations of Stock Exchanges and general case laws govern functioning of all bodies / entities if these bodies / entities, do not have their own rules to govern vicarious liability of these bodies / entities, but if these bodies / entities have their rules for these matters – vicarious liability – in present appeal, then such rules will be applicable.

17. Rule 260 of Bombay Stock Exchange states:-

> <u>Member's responsibility for Partners, Agents and Employees</u>
>
> "A member shall be fully responsible for the acts and omissions of his partnership firm and of his partners, attorneys, agents, remisiers, authorised clerks and employees and if any such act or omission be held by the Governing Board to be one which if done or omitted by the member would subject him to any of the penalties as provided in the Rules, Bye-laws and Regulations of the Exchange then such member shall be liable therefor to the same penalty to the same extent as if such act or omission had been done or omitted by him personally."

18. From perusal of N Sridhar vs. Maruthi Jayaraman case and Rule 260 of BSE regarding Member's responsibility for Partners, Agents and Employee, it can be concluded that no employer can be held for tortious acts of its employees, unless the act of employee was wrongful and authorized by master, which is not the case in present appeal, but when a specific rule of BSE holds stock broker fully responsible for all acts / omissions of its employees, the same must prevail over general principle, enumerated by Hon'ble High Court at Madras. Hence, Stock-Broker (JHP Securities) must be made liable for all acts of its employee Devendra Vadhaiya. This is all the more required since IP was almost 2 years (i.e. August 28, 2006 to August 21, 2008), and during this entire period of 2 years Devendra Vadhaiya executed trades for six clients of Appellant, which were reversal / circular / synchronized, yet Appellant failed to notice the acts of its

employee. It is also admitted that Appellant and all members of stock exchange (Members of Stock Exchanges) are required to scrutinize all trades as per their algorithms on daily basis to find any suspicious activity / trade in their work-stations, yet Appellant did not notice any such activity of its employee, proves beyond doubt that Appellant was negligent in its functioning, to say the least and must be held responsible for all acts of his dealer / employee.

19. As per Ld. AO order, main finding to hold Appellant for violative of regulation 4(1), 4(2)(a) and 4(2)(e) of PFUTP Regulations are:

- Trades were executed by Appellant (from Devendra Vadhaiya terminal in Appellant Andheri office) and Appellant purchased 71,62,146 of GIL (constituting 28.5% of total volume during IP) for its 6 clients and sold 68,40,013 shares (constituting 28.5% of total market volume during IP) for these six clients. These 6 clients were related / connected with each other and with the larger group (NG Group), which included Devendra Vadhaiya, and synchronized, circular and reversal trades were executed. These trades are on record and have not been denied by Appellant.

- Devendra Vadhaiya - who was terminal operator and person-in-charge of a branch of Appellant - had entered into off market trades, with Prem Parekh, during IP.

- Appellant on behalf of its 6 clients entered into synchronized / circular / reversal trades, etc. with NG Group entities during April 24, 2007 to August 21, 2008 (within IP) and NG Group entities accounted for total cumulative Last Traded Price (LTP) increase of Rs. 30 in the scrip i.e. from Rs. 21.80 to 51.80, by executing large number of buy order at price higher than LTP during this phase.

20. Appellant, a stock broker also did not observe clauses A(1) to A(5) of Code of Conduct prescribed and provisions of Stock-Brokers Regulations, which prohibit a Stock-Brokers to create false market or indulge in any act detrimental to investors interest or which leads to interference with fair and smooth functioning of securities market. Stock-Brokers are also required to maintain high standards of integrity, promptitude and fairness and to act

with due skill, care and diligence in conduct of its business. Stock-Brokers are not expected to indulge in manipulative transaction with a view to distort market equilibrium. Since Appellant did not observe above and indulged in synchronized, circular and reversal trades for its clients for a long period of time and created misleading appearance of trading, artificial volumes and price in the shares of GIL, Appellant has been held violative of clauses A(1) to A(5) of Code of Conduct prescribed under provisions of Stock-Brokers Regulations read with regulation 7 of these Regulations and is liable for imposition of penalty under Section 15HB of SEBI Act.

21. In application of Section 15J of SEBI Act regarding factors for deciding quantum of penalty, Ld. AO has held that it is difficult to quantify disproportionate gains or unfair advantage enjoyed by an entity and consequent losses suffered by investors, since investigation report does not deal with this aspect, but keeping in view the practices indulged by Appellant, gains were made by Appellant due to manner of trading in scrip by creation of artificial volumes and liquidity and indulging in price manipulation by increasing LTP, while executing synchronized / reversal / circular trades and these kinds of trades, generate interest of gullible investors in the scrip, being so traded. These kinds of manipulative trades also affect normal price discovery mechanism in securities market. Considering these factors penalty of Rs. 6,00,000/- has been imposed on Appellant under 15HA of SEBI Act for violation of relevant provisions of PFUTP Regulations and Rs. 2,00,000/- under Section 15HB of SEBI Act for violation of relevant provisions of Stock-Brokers Regulations.

22. Considering various aspects of the present case, after perusal of case records and hearing Ld. Counsel for Appellant and Respondent, it is seen that Appellant executed more than 25% of trades in the scrip, both on buy

and sell side during IP (for almost 2 years), for its six clients, namely Prem Parekh, Mala Hemanth Seth, Kishore Chauhan, Hemanth Seth, Bhavesh P Pabari and Ankit Sanchaniya – who are related / connected to one another and are part of larger NG Group – which consists of 17 entities, including six clients of Appellant – and carried out synchronized , reversal and circular trading for its 6 clients, with a view to manipulate volumes in the GIL scrip – thereby manipulate price also by placing orders above LTP in scrip of GIL, when promoters of GIL were finding it difficult to exit, after landing themselves in such a situation, due to acquisition of a sick company and promoters could not revive the company, despite holding shares of same for considerable period of time, the NG Group purchased majority of the shares of promoters – at manipulated excess price than normal market of GIL share, which had not traded for considerable period before IP and was very ill-liquid scrip – and after purchase of majority of shares of GIL from promoters, continued to execute synchronized / reversal / circular trades in scrip of GIL – thus raising the price further and induced gullible investors to invest in the scrip of GIL and made profits for themselves. There was no reason of ill-liquid scrip – which had not been traded since GIL was a sick company – to become liquid and its price to rise, but NG Group entities, increased its liquidity and manipulated price, to give a decent exit to promoters of GIL – in terms of price – and thereafter continued manipulation of volumes and price of GIL scrip, - which induced gullible investors to buy scrip and thus suffer losses, while these clients of Appellant made profit.

23. In the entirety, in execution of a well thought off and well executed plan; Appellant played a crucial role, on behalf of its six clients, in manipulation of volume and price of GIL scrip, but Appellant has tried to

pass the entire blame of these manipulations in GIL scrip during IP on its employee, namely, Devendra Vadhaiya, who is also part of NG Group, and was also branch head of Appellant Andheri office and who executed all synchronized, circular, reversal trades, on behalf of six clients of Appellant, from his terminal.

24. To sum up, dispute in the present case is that, for the offences, if any, committed by an employee of the appellant-broker, whether SEBI is justified in penalising the appellant by imposing penalty of Rs. 6 lac under Section 15HA and Rs. 2 lac under Section 15HB of SEBI Act, 1992. Admittedly, Devendra Vadhaiya, was Andheri Branch in charge and terminal operator of the Appellant. In the ordinary course of business carried on from the said Andheri Branch of Appellant, Devendra Vadhaiya had executed trades on behalf of 6 clients of the Appellant which were found to be synchronised trades, circular trades and reversal trades. Admittedly, all the said 6 clients as also Devendra Vadhaiya have been found guilty of indulging in synchronised, circular and reversal trades and varying penalties have been imposed upon them. Counsel for SEBI stated before us, that all except one of them have paid the penalty imposed against them. Argument of Appellant based on various decisions to the effect that penalty cannot be imposed upon an employer for the offences, if any, committed by an employee, that too based on preponderance of probabilities cannot be accepted in the present case, because Rule 260 framed by the Bombay Stock Exchange specifically provides that a member shall be fully responsible for all the acts and omissions of his partnership firm and of his partners, attorneys, agents, remisiers, authorised clerks and employees. Since synchronised, circular and reversal trades took place from the Andheri Branch of Appellant, in terms of Rule 260 of Bombay Stock Exchange

Rules, Appellant would be liable for penalty. In such a case, yardstick applicable to criminal proceedings cannot be applied and since fraudulent transactions took place from the terminal of the Appellant in the ordinary course of business and since fraud between the 6 clients and employee of the appellant is established, Appellant cannot escape liability. In these circumstances, no fault can be found with the decision of SEBI in imposing penalty upon the Appellant.

25. Accordingly, it is not possible to accept Appellant defence that his employee executed all manipulated trades in GIL scrip, for its six clients, without his knowledge and he has nothing to do with these manipulated trades.

26. In view of this, appeal does not succeed.

Sd/-
Justice J. P. Devadhar
Presiding Officer

Sd/-
Jog Singh
Member

Sd/-
A.S. Lamba
Member

14.10.2014
Prepared and compared by:
msb