WTM/MPB/ISD/162/2020

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA
CORAM: MADHABI PURI BUCH, WHOLE TIME MEMBER
ORDER

Under Sections 11 (1), 11 (4) and 11B (1) of the Securities and Exchange Board of India Act, 1992

In Re: Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003

In respect of:

S. No.	Name of the Entity	PAN
1.	Bharat C. Parekh –HUF	AAAHB0656F
2.	Mansi V. Shah	AADPS1279E
3.	Pravin Somani	AJFPS9670J
4.	Bimal N. Mehta	AAHPM2454K
5.	Jitendra M. Shah – HUF	AADHS0449G
6.	Sanjay J. Shah – HUF	AAFHS6079C
7.	Shimoni S. Shah	BCNPS3115A

In the matter of Front Running Trading activity of Dealers of Reliance Securities Ltd. and other connected entities

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Background

1. Securities and Exchange Board of India's (hereinafter referred to as "**SEBI**") alert system had generated front running alerts for the months of December, 2019 and

January, 2020 against Ms. Meena Ramniklal Vira, suspected to be front running the trades of Tata Absolute Return Fund, a scheme of Tata AIF, a SEBI registered Alternative Investment Fund ("**Big Client / BC**").

2. Based on the aforesaid alert, SEBI conducted a preliminary examination for the period December 1, 2019 to April 15, 2020 (hereinafter referred to as "**Examination Period**") to look into the possible violations of provisions of Securities and Exchange Board of India Act, 1992 (hereinafter referred to as "**SEBI Act**") and various regulations framed thereunder including SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 (hereinafter referred to as "**PFUTP Regulations**") by certain connected entities including Ms. Meena Ramniklal Vira.

SEBI's Examination

3. SEBI's preliminary examination brought out the following:

3.1. It is observed that around 99% of trades of the Big Client in value terms were executed through their broker, Reliance Securities Ltd. ("**RSL**"). At RSL, the Big Client was placing orders through the following 3 Dealers namely, Mr. Harshal Ramnik Vira (Chief Dealer of RSL), Mr. Bhavesh Gandhi (Senior Dealer of RSL) and Mr. Abhijeet Nandkumar Jain (Deputy Dealer of RSL).

3.2. Certain entities connected with the aforesaid Dealers of RSL were *prima facie* observed to have traded depending on the impending orders of the Big Client on numerous occasions during different time periods during the Examination Period. Subsequently, these connected entities squared off their positions when the orders of the Big Client were placed in the market. Thus, they were able to generate substantial proceeds for themselves by placing orders in anticipation of the price movement of scrips on account of large buy / sell orders of the Big Client.

Interim Order

4. In light of the aforesaid findings of the examination, an interim order dated August 7, 2020 (hereinafter referred to as "**Interim Order**") was passed by SEBI *inter alia* against Bharat C Parekh - HUF, Mansi V Shah, Pravin Somani, Bimal N. Mehta, Jitendra M. Shah - HUF, Sanjay J Shah- HUF and Shimoni S. Shah ("**Noticees**"). The interim order against the Noticees was passed taking into account the facts and circumstances described therein, which are, *inter alia*, summarised as under:

   4.1. Mr. Harshal Vira, Mr. Bhavesh Gandhi and Mr. Abhijeet Jain were privy to information with respect to the impending orders of the Big Client as they were the Dealers on behalf of the Big Client for its trades. Thus, they were in possession of information of the impending trades of the Big Client which was not available in the public domain.

   4.2. Noticees are partners in the firm, Labdhi Enterprises ("**firm**"). One of the partners of the firm, Ms. Falguni Ketan Parekh's husband Mr. Ketan Parekh was in communication with Mr. Harshal Vira (3 calls; 1189 seconds) during the Examination Period.

   4.3. The trading pattern of the trades executed from the trading account of the firm was analysed and it showed that the trades executed from the trading account of the firm has followed a Buy-Buy-Sell ("**BBS**") pattern or Sell-Sell-Buy ("**SSB**") pattern around the orders of the Big Client which, as noted from the order log trade log of the firm, was done consistently during the Examination Period.

   4.4. Based on the cumulative effect of various related facts like pre-examination period trading activity of the firm, its common scrip days / contract days with the Big Client and proceeds generated by the firm's trades during the Examination period along with the trading pattern of the firm, it was *prima facie* concluded that the trades executed from the trading account of the firm in the equity derivative segment of the market had 'front run' the orders of the Big Client.

4.5. It was *prima facie* observed that Labdhi Enterprises, Ms. Falguni Ketan Parekh, Bharat C. Parekh –HUF, Ms. Mansi V. Shah, Mr. Pravin Somani, Mr. Bimal N. Mehta, Jitendra M. Shah – HUF, Sanjay J. Shah – HUF and Ms. Shimoni S. Shah, Mr. Harshal Vira and Mr. Ketan Parekh are *prima facie* responsible for the trades executed from the trading account of the firm. It was further, *prima facie* held that the aforesaid entities have violated regulations 3 (a), 3 (b), 3 (c), 3(d), 4(1) and 4(2)(q) of PFUTP Regulations.

4.6. The front running activity of the firm has resulted in *prima facie* benefit to the tune of Rs. 16.97 lakh.

4.7. Based on the aforesaid findings, the following directions were issued against the Noticees:

4.7.1. The Noticees were restrained from buying, selling or dealing in the securities market or associating themselves with securities market, either directly or indirectly, in any manner whatsoever till further directions.

4.7.2. The Noticees were directed to cease and desist from undertaking any activity in the securities market, directly or indirectly, in any manner whatsoever till further directions.

4.7.3. If the aforesaid Noticees have any open positions in any exchange traded derivative contracts, as on the date of the order, they can close out/ square off such open positions within 3 months from the date of order or at the expiry of such contracts, whichever is earlier. The aforesaid Noticees are permitted to settle the pay-in and pay-out obligations in respect of transactions, if any, which have taken place before the close of trading on the date of this order.

4.7.4. The bank accounts of the Noticees to the extent of amount mentioned therein is impounded. Further, the said Noticees are directed to open an escrow account with a nationalised bank, jointly and severally and deposit

the impounded amount of Rs. 16.97 lakh which has been *prima facie* found to be proceeds generated from the *prima facie* front running trades, in the Order, within 15 days from the date of service of the Order. The Noticees shall jointly and severally so deposit the proceeds. The escrow account/s shall be an interest bearing escrow account and shall create a lien in favour of SEBI. Further, the monies kept therein shall not be released without permission from SEBI.

4.7.5. The Noticees, are directed to provide a full inventory of all assets held in their name, jointly or severally, whether movable or immovable, or any interest or investment or charge on any of such assets, including details of all bank accounts, demat accounts and mutual fund investments, immediately but not later than 5 working days from the date of receipt of the order.

4.7.6. The Noticees are directed not to dispose of or alienate any assets, whether movable or immovable, or any interest or investment or charge on any of such assets, held in their name, jointly or severally, including money lying in bank accounts except with the prior permission of SEBI.

4.7.7. The banks where the Noticees are holding bank accounts, jointly or severally, are directed to ensure that till further directions, except for compliance of direction at paragraph 43.4 of the order (currently paragraph 4.7.4), no debits are made in the said bank accounts without the permission of SEBI. The banks are directed to ensure that all the above directions are strictly enforced. On production of proof of deposit of entire amount by any of the Noticees mentioned, in the escrow account, SEBI shall communicate to the banks to defreeze the accounts corresponding to all the Noticees.

4.7.8. The Depositories are directed to ensure that till further directions, except for compliance of direction at paragraphs 43.3 and 43.4 of the order

(currently paragraphs 4.7.3 and 4.7.4), no debits are made in the demat accounts of the Noticees, held jointly or solely.

4.7.9. The Registrar and Transfer Agents are also directed to ensure that till further directions, except for compliance of direction at paragraph 43.4 of the order (currently paragraph 4.7.4), the securities / units held in the name of the Noticees, jointly or severally, are not transferred / redeemed.

5. Vide the aforesaid interim order, the Noticees were advised to submit their replies, if any, within 21 days from the service of the interim order and they were also advised to indicate whether they desire to avail an opportunity of hearing on a date and time to be fixed on a specific request to be made in that regard.

Service of interim order, appeal, reply and hearing

6. The interim order was served on the Noticees vide email dated August 10, 2020. Pursuant to the interim order, the Noticees had filed an appeal (Appeal No. 486 of 2020; Date of decision: December 10, 2020) against the interim order before the Hon'ble Securities Appellate Tribunal ("**SAT**"). The Hon'ble SAT without going into the merits of the case, disposed the appeal with the following directions:

"... the appellants to file their reply / objection on or before December 15, 2020. If such an objection is filed, the WTM will consider the objection and pass a reasoned and speaking order on or before December 31, 2020 after giving an opportunity of hearing to the appellants".

7. Pursuant to the Hon'ble SAT order, vide an email dated December 11, 2020, the Noticees were granted an opportunity of hearing on December 17, 2020 at 4 pm via video conference. In response to the hearing notice and in line with Hon'ble SAT direction, the Noticees vide their letter dated December 15, 2020 submitted a common reply and *inter alia* submitted as follows:

7.1. The Noticees are all merely sleeping partners and have no say in the day to day management of the firm. Ms. Falguni Ketan Parekh is the only working partner as per the partnership deed registered on March 15, 2010 and she is in charge of day to day management of the firm. The only allegation in the interim order is that the Noticees are partners of the firm and are therefore being charged with the *prima facie* observations made in the interim order.

7.2. Ms. Falguni Ketan Parekh is the only partner who draws a salary in the firm. She has opened an account with Canara Bank (Overseas Branch, BKC) bearing no. 1589101020913 and has deposited Rs 17.10 lakh. Thus, the interest of SEBI has been protected.

7.3. Section 25 of the Indian Partnership Act, 1932 ("**IPA**") is a general section applying to "liability" of a partner for the acts of the firm while Section 27 of the SEBI Act deals with the liability of a partner for violation of SEBI Act and the regulations made thereunder. The present case is squarely covered under specific provision of Section 27 (2) of SEBI Act and therefore, the applicability of Section 25 of IPA (which is the general law) is excluded in such cases.

7.4. In order to make a charge against a partner of a firm for the acts of the firm, Section 27 (2) puts the burden on SEBI to establish that the alleged acts are *committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or any other officer of the company.*

7.5. In the present case, it is not even alleged by SEBI that the Noticees were in charge of the firm for the conduct of the business of the firm. Further, the partnership deed and the income tax returns make it clear that the Noticees were not in-charge of the affairs of the firm and had no knowledge of the alleged offence being committed.

8. Noticees vide their common letter dated December 16, 2020 authorised Mr. Ravi Ramaiya, Mr. Kunal Katariya and Mr. Sahebrao Buktare ("**ARs**") to represent them

before SEBI in the extant matter. On the day of scheduled hearing, the ARs reiterated their submissions made in their reply and *inter alia* made the following submissions:

8.1. Noticees are in different line of business than the firm.

8.2. Once Section 27 (1) of SEBI Act is triggered, Section 27 (2) of SEBI Act cannot be invoked. In other words, if the Managing Partner of the firm is held liable, other partners of the firm cannot be held liable.

8.3. The ARs were advised to submit the following information on or before December 21, 2020:

8.3.1. Whether the Noticees were aware that the email id and phone no. given in the KYC form of LFC Securities Pvt. Ltd. ("**LFC**") is that of Mr. Ketan Parekh?

8.3.2. What is the mechanism in the firm to get updates from the working partner? What are the ongoing controls in place on the working of Ms. Falguni Ketan Parekh?

8.3.3. What due diligence has been exercised by the Noticees vis-a-vis the working of the firm?

8.3.4. Who operates the bank account of the firm? The ARs were advised to submit the bank statement of the firm for the period, prior and post 6 months to the Examination Period.

8.3.5. Given the swing in profit figures of the firm over a period of time, the ARs were advised to demonstrate due diligence and control exercised by the Noticees.

8.3.6. What is the qualification of Ms. Falguni Ketan Parekh? The ARs were advised to demonstrate the due diligence exercised by the Noticees before they entered into a partnership with Ms. Falguni Ketan Parekh.

8.3.7. The ARs were advised to submit the demat statement of the firm for the period, prior and post 6 months to the Examination Period.

9. The AR vide his email dated December 22, 2020 while reiterating his submissions made at the time of hearing *inter alia* made the following submissions:

9.1. The email id and mobile no. of the firm as per the records is fparekh@hotmail.com and 9930036340 and the allegation in clauses 23.3.1.1 recording that Labdhi Enterprises and Mr. Ketan Parekh have same email id and mobile no. is incorrect. Likewise, the allegation in clause 23.3.1.2 recording that trade confirmations were being sent to email id and mobile no. of Mr. Ketan Parekh is also incorrect. Copies of sample emails and messages have been submitted by the Noticees.

9.2. It is SEBI's own case that Mr. Ketan Parekh was the alleged information carrier. As partners of the firm, the Noticees had no knowledge of the same and therefore even if SEBI is able to establish the charge under sub-section (1), the proviso to sub-section (1) would negate such charge.

9.3. It is not even alleged in the interim order that the alleged offence was committed with the consent / connivance or attributable to any neglect of any partner. The same is not possible as the present partners being sleeping partners had no role or responsibilities in the firm and therefore the question of applicability of sub section (2) does not apply.

9.4. With respect to ongoing due diligence exercised by the partners, the Noticees have submitted that they meet annually to discuss the results of the firm. The working partner takes care of the day to day functioning of the firm and there is otherwise no meeting of the partners.

9.5. The firm had made a profit of Rs. 5,40,969 in the FY 2017-18 before partners' remuneration, interest and share of profit, while it had made losses in the FYs 2018-19 and 2019-20 to the tune of Rs 11,05,012 and Rs. 16,85,715 respectively. Since returns on investments are inherently inconsistent in securities trading, there is no reason for the partners to expect consistency. Further, the amounts are all in few lakh and therefore are normal.

9.6. Ms. Falguni Parekh is a Diploma Holder in commercial arts and has more than 15 years of experience in financial markets. The dormant partners had invested small amounts looking at her experience.

9.7. The acquaintance with Mrs. Falguni Parekh, her experience in business and the small stakes involved in the investment, collectively were such that the Noticees could pose faith in her.

Findings & Considerations

10. I have considered the allegations levelled against the Noticees in the interim order, oral submissions, their replies/written submissions and other material available on record. I note that in the instant case, the directions issued against the Noticees are interim in nature and have been issued on the basis of *prima facie* findings. SEBI had issued directions vide interim order in the matter in order to protect the interests of investors and the securities market. Detailed investigation in the matter is still in progress. Thus, the issue to be considered at this stage is as follows:

10.1. *Whether in light of the findings of the interim order, the facts and circumstances of the case and the submission of the Noticees in response to the interim order, the directions issued against the Noticees vide the interim order need to be confirmed, revoked or modified in any manner, during the pendency of investigation in the matter?*

I now proceed to consider the aforesaid issue in light of the specific contentions raised by the Noticees.

Issue - *Whether in light of the findings of the interim order, the facts and circumstances of the case and the submission of the Noticees in response to the interim order, the directions issued against the Noticees vide the interim order need to be confirmed, revoked or modified in any manner, during the pendency of investigation in the matter?*

11. Before, I proceed to deal with the Noticees replies/written and oral submissions, it will be relevant to note the following findings of the interim order with respect to the

trades executed from the trading account of the firm for which the Noticees have not made any submissions / disputed. The same are as follows:

11.1. The trades executed from the trading account of the firm have *prima facie* 'front run' the orders of the Big Client.

11.2. The role played by Ms. Falguni Ketan Parekh and Mr. Ketan Parekh in executing the *prima facie* front running trades from the trading account of the firm.

12. It is observed from the submissions made by the Noticees that they have disputed the findings of the interim order only on the following grounds:

12.1. They have no knowledge of the trades mentioned in the impugned order.

12.2. They are not in charge of the firm for the conduct of its business.

12.3. They had no access to non-public information of the Big Client.

13. In support of Noticees submission they have relied upon Section 27 (2) of SEBI Act and have contended that Section 25 of IPA is not applicable in the present case.

14. I note that the *prima facie* finding against the Noticees in the interim order is that they, being the partners of the firm, are *prima facie* responsible, jointly and severally for the acts of the firm.

15. Here, it will be appropriate to reproduce the text of Section 25 of IPA, Section 27 (2) of SEBI Act and regulations 3 (a), 3 (b), 3 (c), 3(d), 4(1) and 4(2)(q) of PFUTP Regulations. The same reads as follows:

IPA

Section 25

Liability of a partner for acts of the firm.

Every partner is liable jointly with all the other partners and also severally, for all acts of the firm done while he is a partner

SEBI Act

27 (2) Notwithstanding anything contained in sub-section (1), where an contravention under this Act has been committed by a company and it is proved that the contravention

has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the contravention and shall be liable to be proceeded against and punished accordingly.

Explanation: For the purposes of this section, —

(a) "company" means any body corporate and includes a firm or other association of individuals; and

(b) "director", in relation to a firm, means a partner in the firm

PFUTP Regulations

3. Prohibition of certain dealings in securities

No person shall directly or indirectly—

(a) buy, sell or otherwise deal in securities in a fraudulent manner;

(b) use or employ, in connection with issue, purchase or sale of any security listed or proposed to be listed in a recognized stock exchange, any manipulative or deceptive device or contrivance in contravention of the provisions of the Act or the rules or the regulations made there under;

(c) employ any device, scheme or artifice to defraud in connection with dealing in or issue of securities which are listed or proposed to be listed on a recognized stock exchange;

(d) engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person in connection with any dealing in or issue of securities which are listed or proposed to be listed on a recognized stock exchange in contravention of the provisions of the Act or the rules and the regulations made there under.

4. Prohibition of manipulative, fraudulent and unfair trade practices

(1) Without prejudice to the provisions of regulation 3, no person shall indulge in a manipulative, fraudulent or an unfair trade practice in securities markets

4 (2) Dealing in securities shall be deemed to be manipulative, fraudulent or an unfair trade practice if it involves any of the following: —

…

(q) any order in securities placed by a person, while directly or indirectly in possession of information that is not publically available, regarding a substantial impending transaction in that securities, its underlying securities or its derivative;

16. One of the submissions of the Noticees is that they do not fall within the ambit of Section 25 of IPA as it is a general law. In this regard, I note that the IPA is not a general law. It is a specific law which deals with the rights, liabilities and duties of the partners vis-à-vis the firm as well as *inter se* among the partners. As noted from the preamble of the IPA, it is "*an act to define and amend the law relating to partnership*". Thus, in a proceeding against a partnership firm and its partners, the first recourse is under IPA as it explicitly lays the provisions governing the conduct of a partnership firm and its partners.

17. At this juncture, I would like to quote the observations of Hon'ble Andhra Pradesh High Court in the matter of *Gattamaneni Prameela and Ors.* vs *Avula Hymavathi and Anr.* decided on June16, 1997. The Hon'ble High Court with respect to the legal liability of the partners, observed as follows:

"…it is true that under the Indian Partnership Act, "firm" or "partnership" is not a legal entity, but merely an association of persons agreed to carry on business. It is only a collective name for individuals carrying on business in partnership. The essential characteristic of a firm is, that each partner is a representative of other partner. Each of the partners is an agent as well as principal. He is an agent insofar as he can bind the other partners by his acts within the scope of the partnership agreement. He is principal to the extent that he is bound by the acts of other partners. In fact, every partner is liable for an "act of the firm". "Act of a firm" has been defined to mean "any act or omission by

all the partners or by any partner or agent of the firm which gives rise to a right enforceable by or against the firm." This is the civil liability of the firm and its partners."

18. In light of the observations made by the Hon'ble High Court, it is noted that the firm as such has no legal recognition but is merely an association of individuals and a firm name is only a collective name of those individuals who constitute the firm. Therefore, for all the acts of the firm, every partner is liable, jointly with all the other partners, and also severally, while he is a partner. This principle is specifically laid down in Section 25 of IPA. Further, Section 25 of IPA does not make a distinction between a working partner and a sleeping partner. Here, it will be appropriate to refer to the observations of Hon'ble High Court of Kerala in the matter of *Ameer and Ors*. vs. *B. Amoo and Brothers and Ors* decided on October 15, 2019, wherein the Hon'ble High Court observed as follows:

    "One of the contentions raised in R.C.R. No. 228 of 2018 is that the person on whose behalf the bona fide need is set up, viz., Smt. Hajira, is a sleeping partner. This expression is not defined in the Partnership Act. In English law, the expression "dormant partner" is used interchangeably for "sleeping partner". Pullock and Mulla on the Indian Partnership Act (7th edition, page 49) makes the following observations:

    "A sleeping partner is nevertheless a partner, even when he only 'sleeps'. Sometimes partners are absolutely inactive or deliberately choose to be inactive, for instance, is some cases where a partner is a government servant or person with similar status who is, by service rules, prohibited from engaging in any trade or business."

    "

19. In view of the aforesaid discussion, I note that for the act of the firm, the liability of the partner, irrespective of whether the partner is a working partner or a sleeping partner, arises from the basic premise that the law identifies the firm by the partners composing it and the principal – agent relationship among the partners. The said principle is expressed in Section 25 of IPA. In the instant matter, for the *prima facie*

act of the firm to 'front run' the trades of the Big Client which was done in the ordinary course of business of the firm (the partnership firm has opened a trading account with LFC in its own name, the partners have authorised Ms. Falguni Ketan Parekh and / or Ms. Mansi V Shah to deal with LFC with respect to dealing in shares / securities and with respect to profits / losses of firm the Noticees have stated that one of the reasons for swing in profit figures of the firm during FYs 2017—20 is that the return on investment are inherently inconsistent in securities trading), the liability to deposit the *prima facie* proceeds of the front running trades, is on all the partners, jointly and severally, by virtue of Section 25 of the IPA. This liability that has accrued to the firm in its ordinary course of business, is the result of loss / injury to the third party which in the given case are the investors in the securities market. Therefore, on the basis of principle as enunciated above (no legal personality of partnership firm and principal – agent relationship among partners), all the partners of the firm are jointly and severally liable to make good for the loss / injury caused to the investors due to the act of the firm.

20. The submission of the Noticees that only Section 27 (2) of SEBI Act is applicable to them as it is a specific law and Section 25 of IPA is not applicable as it is a general law, is not completely accurate. Noticees are correct in submitting that Section 27 (2) is a special law which deals exclusively with the acts / omissions and the consequence thereof, of the firm and its partners in the securities market. In order to arrive at a conclusion on whether or not there is a conflict between the aforesaid two provisions, one has to examine the scope and object of each Section. In other words, is there an apparent conflict between the two independent provisions of law or are they consistent with one another and therefore should be read harmonisously. Section 27 (2) makes a partner in his individual capacity, liable for the act of the firm if the contravention is committed with the consent or connivance or is attributable to any neglect on the part of the partner. The underlying principle of Section 27 (2) of SEBI

Act is not the principal – agent relationship that exists among the partners but the conduct of the partner in the contravention committed by the firm.

21. However, Section 25 of IPA deals with situations where the act of the firm has caused loss / injury to a third party. Before proceeding further, it will be apt to refer to the order of Hon'ble Supreme Court of India in the matter of *Reserve Bank of India* vs. *Peerless General Finance and Investment Co. Ltd.,* 1987 SCR (2) 1 wherein the Hon'ble Court noting the importance of context in the matter of interpretation of statute observed as follows:

"A statute is best interpreted when we know why it was enacted. With this knowledge, the statute must be read, first as a whole and then section by section, clause by clause, phrase by phrase and word by word. If a statute is looked at, in the context of its enactment, with the glasses of the statute-maker, provided by such context, its scheme, the sections, clauses, phrases and words may take colour and appear different than when the statute is looked at without the glasses provided by the context. With these glasses we must look at the Act as a whole and discover what each section, each clause, each phrase and each word is meant and designed to say as to fit into the scheme of the entire Act. No part of a statute and no word of a statute can be construed in isolation. Statutes have to be construed so that every word has a place and everything is in its place."

22. In light of the observations of Hon'ble Supreme Court of India, one has to understand the context of enactment of Section 25 of IPA. Perusal of the IPA as a whole brings to light that liability provisions under IPA have been enacted under two heads; the first is, inter-se liability (indemnity) among the partners and vis-à-vis the firm and the second is, liability of firm towards third parties. The former is not in question in the instant matter. With respect to the second head of liability, reference can be made to Sections 26, 27, 45, 48(b)(i) and 49 of IPA which deal with the liability of the firm towards third parties. Seen in this context, where two kinds of liabilities have been enunciated under IPA, the liability of partners as mentioned under Section 25 of IPA

is nothing but the liability incurred by the firm in the ordinary course of business of the firm due to loss or injury caused to a third party or any debt owed to a third party. Moreover, as discussed earlier, the principle underlying Section 25 of IPA to make the partners liable, jointly and severally, is the principal – agent relationship existing among the partners.

23. The liability of acting partners and non-acting partners (collectively known as firm) for the injury to the third party is an outcome of joint and several liability of such partners under IPA, irrespective of the fact that the conduct (act of the firm) which gave rise to the loss/injury to the third party falls within the definition of "fraud" under securities law. However, a partner who indulges in fraudulent conduct in the securities market, is liable under securities laws also, if his conduct falls within the definition of "fraud". Section 27(2) of SEBI Act creates an additional liability for "fraud" on any partner (other than the one whose conduct falls within the definition of "fraud") if his conduct/omission amounts to consent or connivance to "fraud" or contributed to "fraud". In view of the aforesaid discussion, it is observed that Section 27 (2) of SEBI Act and Section 25 of IPA are not in conflict with each other. Rather, a harmonious reading of both the Sections makes it clear that both the Sections seek to address two different categories of liability.

24. Now I proceed to deal with *prima facie* violation of applicable provisions of PFUTP Regulations. The said provisions deal with 'fraud' in the securities market. Fraud has been defined under regulation 2 (1)(c) of PFUTP Regulations as follows:

"fraud" includes any act, expression, omission or concealment committed whether in a deceitful manner or not by a person or by any other person with his connivance or by his agent while dealing in securities in order to induce another person or his agent to deal in securities, whether or not there is any wrongful gain or avoidance of any loss and shall also include--

(1) a knowing misrepresentation of the truth or concealment of material fact in order that another person may act to his detriment;

(2) a suggestion as to a fact which is not true by one who does not believe it to be true;

(3) an active concealment of a fact by a person having knowledge or belief of the fact;

(4) a promise made without any intention of performing it;

(5) a representation made in a reckless and careless manner whether it be true or false;

(6) any such act or omission as any other law specifically declares to be fraudulent;

(7) deceptive behavior by a person depriving another of informed consent or full participation;

(8) a false statement made without reasonable ground for believing it to be true;

(9) the act of an issuer of securities giving out misinformation that affects the market price of the security, resulting in investors being effectively misled even though they did not rely on the statement itself or anything derived from it other than the market price. And "fraudulent" shall be construed accordingly;

25. Applying the aforesaid definition / requirement of fraud, in the facts and circumstances of the case, the conduct of the Noticees have to be examined. I note that at the interim order stage, based on the *prima facie* material available on record and exigent circumstances, the *prima facie* finding of fraud was rendered against the Noticees as the trades were executed from the trading account which is in the name of the firm and one of its partners, Ms. Falguni Ketan Parekh was connected with the information carrier, Mr. Ketan Parekh (Wife – Husband relationship). These factors coupled with the fact that a partnership firm does not have a separate legal existence but is merely an association of persons who have agreed to carry on a business, it was *prima facie* held that the Noticees have violated relevant provisions of PFUTP Regulations.
26. It is observed from the submission made by the Noticees at this stage that as per the partnership deed, Ms. Falguni Ketan Parekh is in charge of the affairs of the firm.

Further, the Noticees have submitted that they did not have access to non-public information of the Big Client. In this regard, I note that as per the partnership deed, Ms. Falguni Ketan Parekh is the partner who is named as the working partner. Further, an authority letter in her favour along with Ms. Mansi Viren Shah has been executed by the other partners to deal with LFC. Thus, *prima facie,* it is observed that Ms. Falguni Ketan Parekh was managing the affairs of the firm. The interim order has already found that the firm is *prima facie* in violation of provisions related to "fraud" for the *prima facie* front running trades executed from its trading account. Therefore, in view of the new materials brought forth by the Noticees, there is no *prima facie* foundation to observe that there is any act or omission on the part of the Noticees which falls within the definition of fraud. Thus, the *prima facie,* finding of violation of regulations 3 (a), 3 (b), 3 (c), 3(d), 4(1) and 4(2) (q) of PFUTP Regulations against them, at this stage, does not hold good on facts.

27. It is important to note that the front running trade was done by the firm with the money belonging to the firm and the partners would have the right to share the proceeds of the front running trade as the same is property of the firm though earned through means unauthorized by law. As already noted, there is joint and several liability of all partners (collectively known as firm) for the injury/loss to the investors due to the act of the firm. In recognition of that liability the interim order, *inter alia*, has directed the Noticees, jointly and severally deposit the *prima facie* proceeds of front running in an escrow account. The said liability of the Noticees springs from Section 25 of IPA as the same is the result of injury caused to third party, i.e., the investors in the securities market, irrespective of categorisation whether the act of firm is a fraud as defined under securities law.
28. The Noticees have prayed to revoke the directions contained in the interim order. In this regard, I note from the records that Ms. Falguni Ketan Parekh being one of the partners of the firm has *prima facie* deposited the proceeds of front running in an

escrow account of Canara Bank, Overseas Branch, BKC (Account no. 1589101020913) for an amount of Rs. 17.10 lakh with a lien marked in favour of SEBI. Further, as noted in preceding paragraphs, the *prima facie* allegation of violation of PFUTP Regulations against the Noticees at this stage has not been established. Considering that the Noticees have complied with the direction of opening an escrow account and have deposited the proceeds of front running in it, I, therefore, find it to be reasonable to modify the directions issued against them in the interim order.

29. Before proceeding further, it will be appropriate to summarise the findings as noted in the preceding paragraphs:

29.1. The liability of every partner of the firm under Section 25 of IPA is joint and several for all the acts of the firm. The same flows from the principle that a firm does not have legal recognition but is merely an association of individuals and the principle that each of the partners is an agent as well as principal.

29.2. The liability that is addressed under Section 25 of IPA is the liability that has accrued to the firm in its ordinary course of business and has resulted in loss or injury to a third party or any debt owed by the firm to a third party.

29.3. In the given facts and circumstances the Noticees are *prima facie* liable under Section 25 of IPA for the loss / injury caused to the investors.

29.4. There is no conflict between Section 25 of IPA and Section 27 (2) of SEBI Act. The liability under Section 25 of IPA is joint and several on every partner for the injury caused to a third party in the ordinary course of business of the firm irrespective of whether the act of the firm has caused any contravention of securities laws. While Section 27 (2) of SEBI Act creates an additional liability of fraud on an individual partner, if the contravention committed by the firm under securities laws is committed with the consent or connivance of or is attributable to any neglect on the part of the partner of the firm.

29.5. Based on material available on record, at this stage there is no *prima facie* material available on record to indicate that the Noticees have indulged in fraudulent activities in the securities market.

29.6. The investigation in the matter is still in progress which may bring out the omission or commission of the Noticees in the extant matter, if any.

Order

30. Therefore, pending investigation, I in exercise of the power conferred upon me under Sections 11(1), 11(4) and 11B (1) read with Section 19 of the Securities and Exchange Board of India Act, 1992 and in the facts and circumstances of the case, hereby revoke the directions to the extent applicable to the Noticees, given under paragraphs 43.1 to 43.9 in the interim order dated August 7, 2020 with effect from the date of this order. It is reiterated that money kept in the escrow account shall not be released without permission from SEBI.

31. I note that a detailed investigation in the matter is in progress which may bring out additional roles of omission or commission, of the Noticees, if any, in detail, depending on the material and after considering the facts and veracity of their submissions. The findings in the extant order are *prima facie* findings in a matter under investigation.

32. A copy of this order shall be served on all recognized stock exchanges, depositories and registrar and share transfer agents to ensure compliance with the above directions.

DATE: December 30, 2020 **MADHABI PURI BUCH**

PLACE: MUMBAI **WHOLE TIME MEMBER**

SECURITIES AND EXCHANGE BOARD OF INDIA