

BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No. 121 of 2012

Date of decision: 7.8.2012

JHP Securities Pvt. Ltd.
21/28, Gokul Arcade,
S. N. Road, Vile Parle (East),
Mumbai – 400 057.

...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. P. N. Modi, Advocate with Mr. Vinay Chauhan, Mr. Naville Lashkari and Mr. Anant Upadhyay, Advocates for the Appellant.

Dr. Poornima Advani, Advocate with Mr. Omprakash Jha, Advocate for the Respondent.

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

Per : S.S.N. Moorthy

The present appeal is directed against an order passed by the whole time member of the Securities and Exchange Board of India (for short the Board) under section 19 of the Securities and Exchange Board of India Act, 1992 (the Act) read with regulation 28(2) of the Securities and Exchange Board of India (Intermediaries) Regulations, 2008 (referred to hereinafter as Intermediaries Regulations). Acting under regulation 28(2) read with regulation 38(2) of the Intermediaries Regulations the whole time member suspended the certificate of registration of the appellant for a period of one month on May 11, 2012.

2. The appellant is a stock broker on the Bombay Stock Exchange Ltd. having certificate of registration granted by the Board. The Board conducted investigation in the dealings of Shri J.E. Talaulicar (Talaulicar) in the shares of Tata Finance Ltd. (Tata Finance) for the period September 2000 to March 2001. Investigation related to insider trading indulged in by Talaulicar in the shares of Tata Finance. The Board initiated

enquiry proceedings against the appellant in terms of Securities and Exchange Board of India (Procedure of Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002. A show cause notice was issued to the appellant on November 5, 2004 alleging that it had acted as a conduit along with sub broker J. I. P. Investments P. Ltd. (JIP or sub-broker) to enable Talaulicar to siphon off funds of Niskalp Investments Trading Company Ltd. (Niskalp) of which he was the chairman. Accordingly, it was alleged that the appellant was guilty of violating provisions of clauses A(1), (3) and (5) and B(1) and (2) of Schedule II of code of conduct for stock brokers under regulation 7 of Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1992 (Takeover Regulations). The appellant sought adjournments from time to time citing various reasons. The proceedings spanned over a considerable period of time and in April 2012 written submissions were filed by the appellant. In the written submissions, the appellant denied the allegation and submitted that various documents and submissions asked for by it were not provided. According to the appellant opportunity to cross examine persons whose statements were recorded by the Board was also not afforded. On the whole, the appellant contended that in the absence of all the relevant documents and statements asked for from the Board the allegations could not be satisfactorily answered and submitted it had no role as alleged in the show cause notice in the transfer of funds to Shri Talaulicar in a fraudulent manner.

3. The whole time member, after due consideration of the show cause notice and the material on record framed the following 3 issues for consideration in the present case.

- a. “Whether the noticee broker acted as a conduit for the transfer of funds from NITCL to Talaulicar and later for the refund of the amount by Talaulicar to NITCL in violation of the provisions of Clauses A(1), (3) and (5) of Schedule II of the Code of Conduct for Stock Brokers under Regulation 7 of SEBI (Stock Brokers and Subbrokers) Regulations, 1992 read with Regulation 4 of SEBI (Insider Trading) Regulations, 1992 and Regulation 4(c) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to the Securities Market) Regulations, 1995?
- b. Whether there were deficiencies in client registration and client agreement maintained by the noticee, in violation of SEBI Circular SMDRP/POLICY/CIR/5-97 dated April 11, 1997?
- c. Whether the noticee broker delayed making payments to NITCL, in violation of Clause B (1) of the Code of Conduct as specified in Schedule II, read with Regulation 7 of SEBI(SB&SB) Regulations, 1992 and SEBI Circular SMD/SED/CIR/93/23321 dated November 18, 1993?”

He also concluded that the appellant had been provided with all the documents relied upon in the investigation and since reliance has not been placed on any statements there was no scope for cross examination of parties. After analysing the issues framed above and considering the submissions made by the appellant, the whole time member concluded that there was violation of the impugned regulations and so suspension of certificate of registration for one month was warranted. Hence this appeal.

4. The first issue that arises for consideration is the transfer of funds from the appellant to the sub broker and back to Talaulicar and the role of the appellant in this transaction. The relevant facts of this transaction as noted by the whole time member are the following: The appellant who was acting as a broker of Niskalp received an amount of ` 70 lacs from Niskalp on March 30, 2001. Already there was a credit balance of ` 83 lacs relating to Niskalp in the books of the appellant. On March 31, 2001 appellant transferred ` 69 lacs to sub-broker. The proprietor of the sub-broker company, in turn, issued cheques dated March 30, 2001 to Shri Talaulicar and his family members under the guise of sale transaction of 1 lac shares of Tata Finance relating to September 2000. The sub-brokers' account was debited on April 4, 2001 and April 7, 2001. Shares were transferred to the sub broker's account on April 4, 2001. According to the whole time member, Talaulicar and his family members received a consideration of ` 69 lacs on March 30, 2001 though the actual sale of shares took place in May, 2001 for a consideration of 34.21 lacs. In September 2000 the ruling price of the share was ` 69/- whereas in March 2001, it came down to ` 40/-. Thus, Talaulicar and family received a consideration of ` 69 lacs as relating to the share price prevalent in September 2000 even though real transaction took place much later in May 2001. Of course, the excess amount of 34.79 lacs was transferred by Talaulicar to the sub broker between May 2001 and June 2001. In 2001, the sub broker transferred ` 69 lac to the appellant who, in turn, transferred ₹ 153 lac to Niskalp since it did not effect any purchases. The whole time member concluded that the appellant, by transferring a sum of ` 69 lac to the sub broker, which, in turn, transferred the money to Talaulicar, was acting as a conduit in the whole process and so there was violation of the code of conduct for stock brokers.

5. We have heard Shri P.N. Modi, learned counsel for the appellant who took us through the records of the case. With reference to the records of the case and the account statements, it is emphatically argued by him that the appellant cannot be held responsible or privy to the arrangement between Talaulicar and the sub broker since the appellant had not done any trade for or on behalf of Talaulicar. The appellant was a broker for Niskalp and there was a running account between the two which contained substantial credit balance. In the normal course of business Niskalp used to keep credit balance with the appellant to meet the various margin requirements as a precaution to meet the heavy pay out requirements. Niskalp paid a sum of ` 70 lacs to the appellant towards meeting such margin requirements and advance for future purchase and there was nothing irregular or suspicious since it was the practice of Niskalp to make heavy periodical payments to the appellant. The appellant paid ` 69 lacs to the sub broker since the sub broker demanded the amount out of the sum receivable by it from the appellant. According to the appellant it was only a routine payment in the course of its business transactions with the sub broker. It is specifically submitted that the subsequent payments made by the sub broker is none of the appellant's concern since the appellant had no dealings with Talaulicar. It is submitted that the appellant was a broker for Niskalp and JIP was its sub broker and the dealings were confined to normal share trading and connected payments and there is no intention, let alone, any evidence to point to any inference that the appellant willingly acted as a conduit. The transfer of a sum of ` 70 lacs from Niskalp to the appellant cannot be regarded as abnormal in the background of periodical transactions between them and the payment made to sub broker cannot, by any stretch of imagination, be tagged on to the above sum of ` 70 lac. With reference to the accounts maintained by the appellant it is submitted that the receipt from Niskalp on various days is of an adhoc nature and it is not a bill to bill payment strictly relating to the purchase of shares for Niskalp. It is also categorically pointed out that there is a missing link in so far as the return of funds to the appellant as observed by the whole time member is not established.

6. Apart from the merits of the case mentioned above, the appellant's learned counsel very strenuously argued that relevant documents and statements relied upon by the whole time member have not been provided to the appellant in spite of several requests and the

stand taken in the impugned order with regard to the said documents and statements is untenable. According to the appellant's learned counsel, submissions made by Talaulicar are central to the investigation report which forms the basis of the impugned order. The failure to provide the statements and submissions relied upon by the whole time member is a basic infirmity and it goes to the foundation of the impugned order.

7. Dr. Poornima Advani, learned counsel appearing for the Board, strongly supported the order of the whole time member. According to her, the appellant resorted to protracted delaying tactics in replying to the show cause notice and in personal hearing and the whole time member was constrained to proceed with the case on the basis of some of the submissions made by the appellant and the facts emerging from the records. According to the learned counsel for the Board, there is no denial of natural justice since all documents relied upon in the investigation have been provided to the appellant and there was no need for any cross examination of parties in the absence of any submissions being relied upon. With reference to the account statements maintained by the appellant it is submitted that the payment of the impugned sum of ` 70 lacs is abnormal since most of the debits and credits in the statement relate to specific purchase of securities and settlement thereon. There was no need to make substantial periodic payments to the appellant since the margin required as per guidelines was only about 20 per cent and the account showed substantially higher amount. Therefore, there was no need for the payment of a hefty sum of ` 70 lacs. According to the Board, the story of maintaining a substantial balance in the account for a future project is farfetched and there is no evidence of any future crystallized project. There was no need to provide the appellant with a heavy amount especially when the company was running at a loss. The proximity of days of the credit of adhoc margin of ` 70 lacs and the pay out and the subsequent payment by the sub-broker to Talaulicar clinches the issue as one of a preplanned siphoning off of funds. The appellant has not raised any dispute regarding the voucher of ` 70 lacs issued by Niskalp and also about the flow of funds. The funds were called back from the appellant by Niskalp only after June 2001, when the transactions between the appellant, sub broker and Talaulicar were settled. The impugned transactions between the sub broker and Talaulicar with respect to purchase of shares leave considerable room for

suspicion. The amount of ` 69 lac transferred from the sub broker to Talaulicar is said to be relating to share price of previous dates as different from the share price prevailing in March 2011. The subsequent modification of the transaction and refund of the amount to the sub broker establishes the game plan of the group. With reference to the account statement and the transactions connected thereto the learned counsel for the Board would submit that the appellant has received and transferred the impugned amount in unusual circumstances facilitating the manipulative intent of Talaulicar.

8. We have considered the rival submissions. It is true that the appellant had dragged the proceedings considerably in this case at the stage of reply to the show cause notice and personal hearing. However, the appellant submitted a reply to the show cause notice on June 27, 2005 in which specific reference was made to the request for certain statements and documents relating to investigation report which is the basis of the impugned order. Among other things, the appellant asked for copies of statement or submission of Shri Talaulicar, M/s. JIP Investment, Shri Bharat Patel etc. There is no gain saying the fact that the entire proceedings emanated from an investigation report relating to insider trading in the scrip of Tata Finance. The investigation report is part of the appeal papers filed by the appellant. In the investigation report there is reference to the 'submissions' made by Shri Talaulicar in various places. It has to be inferred that Shri Talaulicar has supplied certain information to the investigating officer. The 'submissions' referred to in the investigation report may normally be in the form of a statement given by Talaulicar. In the enquiry proceedings conducted on July 8, 2003 the appellant was provided with a few documents like copies of sub brokers' deals, copies of voucher of Niskalp, copies of cheque issued to Talaulicar etc. However, the investigating officer was silent about copies of statements or submissions of Talaulicar. In the written submissions dated January 27, 2005 the appellant invites the attention of the Board to its previous letters dated 26.4.2003 and 12.6.2003 in which specific request was made for certain documents and statements. In the impugned order the whole time member has observed that the appellant had been provided with all documents relied upon in the investigation and no submissions are relied upon and, therefore, there is no need for any cross examination. On an examination of the specific request made by the appellant and the reference made in the investigation report

we are of the view that the submissions of Talaulicar are crucial to the proceedings in this case. Admittedly, the investigation report has been provided to the appellant. However, the submissions of Talaulicar and other connected persons on the basis of which the investigation report is prepared have not been provided to the appellant. Since the submissions of Talaulicar go to the root of the investigation the whole time member could not have shut his eyes on the request of the appellant to provide copies of the same. In the investigation report, which is part of the records, a detailed analysis of the chronology of events leading to the sale of shares by Talaulicar and family is carried out. “The submissions of Talaulicar” forms the basis of the aforesaid analysis and it is mentioned so in various places. In view of the fact that the investigation report relies heavily on the submissions of Talaulicar in various places the appellant should have been provided with the same in the interest of natural justice. It goes without saying that it is incumbent upon an authority to provide the delinquent with all the basic facts and submissions made by other parties which are relied upon by him in the proceedings. To this extent, requirements of natural justice have not been complied with in the present case.

9. Now, let us examine the facts of the case so as to find out whether the conclusion drawn by the adjudicating officer is based upon proper reasoning and reliable evidence. It is not disputed that the appellant was acting as the broker of Niskalp and JIP Investments was the sub-broker of the appellant. The appellant has on-going transactions with Niskalp and the account statement furnished by the appellant establishes periodical, substantial flow of funds. It is also an admitted fact that the appellant had no transactions whatsoever with Talaulicar, even though Talaulicar was the chairman of Niskalp. From a perusal of the account statement, it is noticed that the fund flow was not strictly in accordance with bill to bill payment but there were several adhoc receipts and payments. Since Niskalp acted with Tata Finance and the appellant had to purchase shares of a substantial order, as and when there was availability, the appellant had heavy credit balance in its accounts. It is evident from the account statement that Niskalp had transferred ₹ 70 lacs to the appellant on March 30, 2001. A verification of the account statement, which is on the record, would show that some of the payments can be closely related to purchase of shares for Niskalp whereas there has been several instances of adhoc receipts from Niskalp which the

appellant used to keep as margin money. The appellant has acted as a broker, pure and simple. The appellant stated the factual position upfront in the initial reply filed by it. It runs as under-

“it is submitted that as stated hereinbefore, we had no dealings with Mr. Talaular as a broker or otherwise. Further, it is submitted that we had never met him and we had never received any instruction from him even on behalf of NITC. It is submitted that we were not aware that he had received any excess consideration, or that he had refunded any amount to our sub-broker as alleged. It is submitted that we had no knowledge of dealings between sub-broker and Mr. Talaular since these were independent transactions carried out by them in their individual capacities. Further, in the absence of any involvement on our part in the said dealings between sub-broker and Mr. Talaular, cannot be attributed to us merely on surmises and suspicions de hors of any supporting evidence.”

10. It requires reiteration that the appellant had no dealings with Talaular. The appellant transferred ₹ 69 lacs to sub-broker, JIP by way of settling accounts with the sub-broker. The receipt from Niskalp and the out go to JIP is, in the facts of the case, a normal business transaction between a client, broker and sub-broker. It may be true that the sub-broker transferred funds to Talaular on receipt from the appellant. As long as there were no dealings between the appellant and Talaular the transactions between the sub-broker and Talaular cannot point a finger at the appellant. The whole time member has taken objection to the transfer of funds by way of adhoc margin to the appellant in as much as sufficient funds were lying unutilized in the appellant's accounts. We cannot question the logic of Niskalp in transferring funds to its broker by way of adhoc margin. In fact, it is for the client and the broker to decide how much funds should be transferred and when it has to be utilized. However, in the circumstances of the present case, the flow of funds from Niskalp to the appellant was large in volume and the transfer of funds when sufficient credit balance was lying with the appellant cannot, by itself, lend any suspicion. There is considerable merit in the submission of the appellant that the action of the sub-broker in transferring the funds to Talaular is of no material concern to the appellant. Thus, the flow of funds as appearing in the present case has to be regarded only as one which took place in the normal course of business activity.

11. The appellant has given a specific reply to the allegation of siphoning off funds contained in the show cause notice. The appellant's reply is quoted for ease of reference:-

“11.2.1 We wish to point out that we are not aware of the any payment and/or transaction between JIP Investments and Mr. J.E. Talaular being subject matter of SCN. While it is correct that we paid NITCL towards their credit lying with us as the same was called for by them at that period of time and they had informed us to return the same as they had no desire of any further trading and/or investment or purchases after the Index was continuously falling for the reasons known to all concern. In fact, we returned to NITCL a sum of Rs. 1.53 crores which was lying in our account of NITCL as credit balance/margins;

11.2.2 In would be incorrect to conclude that we acted as conduit for the return of fund to NITCL as our dealings with NITCL have been in the normal course of business. The amount of Rs.1.53 crores which was paid by us in May-June, 2001 to NITCL was not received by us from JIP. In fact, no significant amount was paid to us by JIP during May-June, 2001.”

12. The whole time member has given his finding, thus:-

“vii. On examination of the facts of the case and the explanations offered by the noticee broker, I find it unlikely that the chain of transfer of funds, to and from NITCL to JHP to JIP and then to Talaular is a sequence that occurred by chance. The amounts received by the noticee from NITCL and the amount transferred by it to JIP are almost the same. The transfer also took place merely a day apart. On the other hand, the subsequent receipt of money by the noticee from JIP and payment to NITCL was again closely matched. It is highly unlikely that both tranches of the transactions, if independent of each other, could be so closely linked in terms of amount and dates. The contentions of the noticee seem to be a belated attempt to cover up the transgression.

viii. In view of the forgoing, it appears that the noticee broker acted as a conduit for the transfer of funds from NITCL to Talaular and later for the refund of the amount by Talaular to NITCL.”

13. It is interesting to note that while arriving at the finding the whole time member has observed that “it appears that the noticee broker acted as a conduit”. It is clear that the whole time member is not categorical or specific in his finding.

14. The learned counsel for the Board submitted that payment of adhoc margin of substantial sums cannot be regarded as a normal business process. It was also submitted by her that Niskalp was passing through financial difficulties and it had not made profits during the relevant period and in that background payment of huge amounts to the broker arouses suspicion. It was also pointed out that the story of providing money to the broker for a significant future project is farfetched in as much as there were no heavy purchase of

shares after the impugned period. According to her, maximum possible evidences were correlated with reference to the facts of the case and the transactions and the appellant was definitely acting as a conduit. As regards the transactions, as borne out of the account statements, we have to observe that the flow of funds by itself does not render any suspicion in the present case. Proximity of dates relating to transfer of funds may not also lead to any serious consequence since the appellant cannot be rendered accountable for the actions of sub-broker who had custody of the funds. The financial status of Niskalp is also not material since the payment made to the broker is an asset and can be recovered at any point of time. In fact, the appellant returned a sum of ₹ 153 lac to Niskalp as and when demanded and this evidences the business relationship between Niskalp and the appellant. We are unable to read anything more than what is apparent in these transactions.

15. It is true that market manipulation can be proved only through circumstantial evidence and preponderance of probabilities. However, a competent authority has to place on record proper, logical and reasonable evidence to establish a case of preponderance of probabilities. Every finding of the competent authority must be based on an independent appraisal of evidence on record and he cannot be allowed to be influenced by peripheral possibilities in a case. In the present case, the finding given by the whole time member which has been mentioned supra clearly establishes that there was no appraisal of necessary evidence which could clinch the issue of manipulative dealings between the appellant and Talaulicar.

16. In the facts of the present case it is also worthy of mention that the return leg of the transaction between the sub-broker and the appellant as alleged is not established. It is stated by the appellant that the allegation regarding return of ₹ 69 lacs between April 1, 2001 and June 30, 2001 to the appellant is not borne out of facts. Obviously, the appellant cannot be faulted if funds had been transferred by Talaulicar to the sub-broker in the relevant period. A reading of the impugned order shows that the whole time member has relied heavily on the return leg of the transactions. The appellant has annexed a copy of the receipts from the sub-broker during the period April 1, 2001 to June 30, 2001.

Similarly, payment made by the appellant to Niskalp during the above period is also annexed. However, the return of funds as concluded by the whole time member is difficult to be traced in the transactions contained in the annexure. So, the chain of events on which the whole time member has placed his findings cannot be regarded as one which suggests a manipulative intent on the part of the appellant. Mere conjectures and correlation of certain events without reasonably good evidence to support the allegation cannot bind a person to the charge of market manipulation.

17. The learned counsel for the Board placed reliance on the decisions of this Tribunal in the case of Avadhoot L. Shilotri vs. SEBI, Appeal no. 31 of 2004 dated 21.5.2004 and Dilip S. Pendse vs. SEBI, Appeal no. 90 of 2007 dated 20.11.2008. These decisions may not be of any help to the Board since the basic charge in those cases related to insider trading. There is also no reference to the appellant or its role in those decisions. So we are not in a position to identify any linkage between the appellant in the present case and the appellants in those decisions.

18. Suspension of certificate of registration of a broker is a matter of serious concern and even if it is for a period of one month it has far reaching consequences as far as a broker is concerned. Such drastic action necessarily calls for establishment of a case of serious violation or non compliance. In view of the discussion above, we are of the view that there is no case to draw an adverse inference against the appellant based on the transfer of funds which took place in the present case and so no case of serious violation as alleged stands established.

19. The whole time member found fault with the appellant with respect to deficiencies in client's registration and agreement maintained by the appellant in respect of SEBI's circular dated April 11, 1997. However, on a perusal of the findings in the impugned order, we are of the view that no serious charge has been made out and the deficiency pointed out does not call for any penal action since it required only modifications/corrections in the documents contained. At any rate, no serious wrong doing arising out of the above allegation has been made out.

20. The whole time member found the appellant guilty of violation of SEBI circular dated November 18, 1993 with regard to making payments to the clients. The appellant has been found fault with for the adjustment of debit and credit in the accounts without proper authority in this regard. However, we find that no serious wrong doing has been made out and the ledger accounts properly evidence authority given to the appellant and there is no complaint whatsoever regarding delivery and payment.

In view of the discussion above, we set aside the order of the whole time member, allow the appeal with no order as to costs.

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

Sd/-
S. S. N. Moorthy
Member

7.8.2012

Prepared and compared by
RHN/PTM