

IN THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No. 97 of 2004

Date of decision : 4.5.2007

K.N. P. Securities Pvt. Ltd. **Appellant**

Versus

Securities and Exchange Board of India **Respondent**

Mr. Prateek Seksaria Advocate with Mr. Deepak Shah Advocate for the appellant.

Mr. Kumar Desai Advocate and Ms. Daya Gupta Advocate for the respondent.

Coram : Justice N.K. Sodhi, Presiding Officer
R.N. Bhardwaj, Member

Per : Justice N.K. Sodhi, Presiding Officer

This order will dispose of two Appeals nos. 97 & 100 of 2004 which were heard together and involve common questions of law and fact. Learned counsel for the parties are agreed that the decision in one will govern other appeal as well. Since arguments were addressed in Appeal no. 97 of 2004, the facts are being taken from this case.

M/s. KNP Securities Private Limited the appellant before us had been operating as a stock broker in the securities market and was registered with the Securities and Exchange Board of India (for short

the Board). In view of the allegations of price manipulation in the scrips of some companies, the Board carried out investigations. Investigations revealed prima facie the involvement of one Mr. Ketan Parekh and some companies including the appellant controlled by him and connected to him in manipulating the market in respect of certain scrips. An ex-parte order dated April 10, 2001 was passed by the Board debarring the appellant along with M/s. V.N. Parekh Securities Private Limited (the appellant in Appeal no. 100 of 2004) from undertaking any fresh business as stock brokers till further orders. This order was confirmed on June 21, 2001 after affording a post decisional hearing to the parties. By the same order, an enquiry officer was appointed against all the broking entities of Ketan Parekh including the appellant to enquire into the alleged violations of the Securities and Exchange Board of India Act, 1992 (for short the Act) and the regulations made thereunder. The enquiry officer found that the appellant had not indulged in any manipulative trading in any of the scrips as alleged in the show cause notice read with the enquiry report and that such instances were negligible in scrips of some of the companies and nil in others. He, however, found that Ketan Parekh was a director of the appellant company and was the person who looked after its day-to-day activities and on this account, it was observed that the appellant was not a fit and proper person to carry on business as a stock broker. He referred to the guidelines issued by the Board in regard to the fit and proper persons. Since he had

recommended the cancellation of certificates of registration of various companies which were being controlled by Ketan Parekh, he was of the view that the certificate of registration of the appellant, too, should be cancelled as it was also being controlled by Ketan Parekh. The enquiry officer was of the opinion that if all the entities belonging to Ketan Parekh were not debarred from accessing the capital market, he may operate through the entities which were not debarred. He, therefore, recommended the cancellation of the certificate of registration of the appellant as well, as, according to him, the appellant was not a fit and proper person to operate in the securities market owing to its close association with Ketan Parekh. It is pertinent to mention here that by order dated 12.12.2003 passed by the Board Ketan Parekh and his brother Kartik K. Parekh along with their investment companies had been debarred from accessing the capital market for a period of 14 years for having rigged the securities market by manipulating the scrips of some of the companies in a big way and that order has been upheld by this Tribunal on 14.7.2006.

On receipt of the enquiry report the Board issued a notice dated January 31, 2003 to the appellant calling upon it to show cause why penalty be not imposed in terms of the Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Regulations, 1992 (for short the Regulations). A copy of the inquiry report was also sent along with the notice. Admittedly, the appellant did not file any reply to this

show cause notice. The Board after affording an opportunity of personal hearing to the appellant concurred with the findings of the enquiry officer that the appellant was not a fit and proper person to operate in the securities market because of its association with Ketan Parekh and cancelled its certificate of registration as a stock broker by order dated March 8, 2004. It is against this order that the present Appeal and Appeal no. 100 of 2004 have been filed.

We have heard the learned counsel for the parties. The first contention of the learned counsel of the appellant is that the ground on which the certificate of registration of the appellant has been cancelled did not form part of the show cause notice and, therefore, the appellant was not given an opportunity to meet the charge that it was not a 'fit and proper person' to operate in the securities market. We are unable to accept this contention. The show cause notice dated January 31, 2003 was issued to the appellant and it was stated therein that the enquiry officer had found it "guilty of having violated provisions of SEBI (Stock Brokers and Sub-Brokers) Rules and Regulations, 1992 read with the provisions of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to the Securities Market) Regulations, 1995. Accordingly, the enquiry officer has recommended that the registration granted to you be cancelled. A copy of the Enquiry Report is enclosed." The appellant was called upon to show cause why penalty as considered appropriate be not

imposed on it. The enquiry officer in his detailed report while referring to the appellants in these two appeals had observed as under:

“As regards other noticees namely VN Parekh Securities and KNP Securities. I find that the instances of manipulative trading in the scrip under the show cause notices are negligible as nil in some cases. I find that Shri. Ketan Parekh is a Director and is the person who looks after day to day activities of these noticees. I find that fit and proper criteria is one of the important criteria for a stock broker. The SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992 dealing with the grant of registration to the intermediaries provide for the concept of “a fit and proper person”. In terms of which no applicant shall be given a certificate of registration unless it fulfils the eligibility criteria of being a fit and proper person.”

The enquiry officer then referred to clauses (a) to (g) of the guidelines laid down by the Board for determining whether an applicant was a fit and proper person and made the following recommendation –

“In my opinion if all the entities belonging to Ketan Parekh are not debarred from capital market, he may operate through the entities which are not debarred. The recommendation for cancellation of registration against TSL, NH Securities, CSSB, TIFL, will not be effective unless similar order is passed against VN Parekh and KN Parekh. He may therefore operate through VNP and KNP, if their licences are not cancelled. In my view, such persons should not be allowed to operate in securities market at all. Taking into consideration all the facts and circumstances, I also recommend cancellation of registration certificate of VNP Securities and KNP Securities. Taking into consideration all the facts and circumstances, I also recommend under regulation 28(7) of Stock Broker Regulations read with regulations 5(e) of Stock Broker Regulation, cancellation of registration certificate of VNP Securities and KNP Securities.”

Admittedly the appellant did not file any reply to the show cause notice nor to the observations made by the enquiry officer in his report. The Board, however, afforded a personal hearing to the appellant before passing the impugned order. The appellant after appearing in person through its representative submitted its detailed written submissions to the Board. It is true that the show cause notice did not specifically state that the appellant was not a fit and proper person though reference was made to the Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Rules and Regulations, 1992 but the show cause notice did not contain any facts and reference therein was made to the findings recorded by the enquiry officer and a copy of the enquiry report was sent along with the notice. It would have been better if the Board had specifically made out the charge in the show cause notice itself but the practice which was then in vogue with the Board was not to frame charges in the show cause notice and instead a copy of the enquiry report containing all the allegations against a market intermediary was sent along with a show cause notice to which the intermediary was required to file its reply. The same practice was followed in the instant case. In the circumstances of the case the enquiry report would be treated as an integral part of the show cause notice to which the appellant was required to file its reply. Instead of repeating in the show cause notice the allegations and findings that they were made in the enquiry report, the Board chose to send the complete enquiry

report to the appellant to file its reply. We cannot hold that the principles of natural justice were not followed or that there was any infirmity in the show cause notice. We have perused the written submissions filed by the appellant and it is clear therefrom that it clearly understood the charge that it was required to meet and it is not a case where the appellant was taken by surprise or that the findings against it were recorded for the first time in the impugned order. The enquiry officer clearly stated that in view of Regulation 5(e) of the aforesaid Regulations and for other reasons stated therein the appellant was not a fit and proper person. Regulation 5(e) of the aforesaid Regulations provides that an applicant shall not be granted a certificate of registration if it was not a fit and proper person and this criteria it must continue to satisfy throughout the period of validity of its registration and throughout the period it associates with the securities market. Further, when we look at the memorandum of appeal filed by the appellant we find that no specific plea has been taken therein that the charge of not being a fit and proper person was not contained in the show cause notice. On the other hand the appellant has tried to justify in the grounds of appeal that the allegation made was not justified. In this view of the matter we have no hesitation in rejecting the first contention raised on behalf of the appellant.

The next contention of the appellant is that the Board grossly erred in relying on Securities and Exchange Board of India (Criteria for Fit and Proper Person) Regulations, 2004 for holding that the appellant was not a fit and proper person. The argument is these Regulations came into force on 10.3.2004 whereas the cause of action in the present case had arisen much prior thereto and, therefore, the impugned order deserves to be set aside on this ground alone. The argument advanced before us is misconceived. There is no reference to these regulations in the impugned order. The Board has, in the impugned order, relied upon the criteria of fit and proper person as laid down by it in its guidelines which were framed in the year 1997-98. Regulation 5 of the Stock Brokers Regulations, 1992 provides for the matters to be considered by the Board for the grant of a certificate of registration to a stock broker. Clause (e) was inserted therein with effect from 5.1.1998 which provides that one of the matters to be considered by the Board is whether an applicant is a fit and proper person. The term 'fit and proper person' had not been defined and the Board framed its guidelines providing for the criteria determining whether an applicant was a fit and proper person or not. One of the criteria is contained in clause (g) of the guidelines which provides for any other reason to be recorded in writing by the Board which adversely affects the reputation or the character of the applicant and has a bearing on the capital market so as to deny the applicant certificate or renewal thereof. Instead of mentioning clause (g) of the

guidelines in the impugned order the Board seems to have mentioned clause (f) through some inadvertence and the appellant seems to be taking advantage of this typographical error. If we read criteria (g) for criteria (f) as mentioned in paragraph 7.6 of the impugned order it becomes clear that the Board has found the appellant not to be a fit and proper person because of its association with Ketan Parekh as it has recorded finding that the appellant was being controlled by Ketan Parekh in its day-to-day affairs. When faced with this situation the learned counsel for the appellant urged that the guidelines have no statutory force and, therefore, could not be relied upon by the Board. This contention of the appellant is being noticed only to be rejected. When clause (e) was inserted in Regulation 5 of the Stock Brokers Regulations, 1992 there was no criteria on the basis of which the Board could judge an applicant to be a fit and proper person. The Board then framed the guidelines in question for its internal use which find mention in its annual report for the year 1997-98 which was placed before the parliament. It is not the case of the appellant that these guidelines had ever been flouted. It was necessary to have these guidelines so that there was uniformity in its decision in judging the different clauses for registration as market intermediaries. Absence of guidelines could have exposed the Board to the charge of discrimination / arbitrariness. The Board is a statutory regulator of the securities market and the statute creating it has enjoined upon it the duty to protect the interest of investors in the securities and to promote

the development of and to regulate the securities market by such measures as it thinks fit. The guidelines framed by the Board were a part of the regulatory measures which it took in the absence of any statutory provision. The statutory Regulations of 2004 came into force with effect from 10.3.2004 and from then onwards the guidelines have given way to the statutory regulations.

Lastly, it was urged on behalf of the appellant that it was a body corporate quite distinct from Ketan Parekh and his other investment and broking companies and enjoys the status of a separate legal entity and, therefore, the Board was in error in cancelling its certificate of registration merely because of its association with Ketan Parekh. We are not impressed with this argument. It is true that the appellant is a body corporate which is distinct from Ketan Parekh and his other legal entities but when serious allegations of market manipulations are levelled against the appellant and those entities, it is legitimate to lift the corporate veil and find out who is the person acting behind the curtains. When we do that in the case of appellant, we find it is Ketan Parekh who is running the show. In paragraph 6.2 of the impugned order the Board has given detailed reasoning for holding that it was Ketan Parekh who was carrying the day-to-day activities on behalf of the applicant. None of those findings has been challenged before us and, therefore, we cannot accept the contention that merely because the appellant is a body corporate distinct from

Ketan Parekh and his other companies, it should be allowed to operate as a stock broker in the market. It is pertinent to mention here that by a detailed order dated 12.12.2003 passed by the then chairman of the Board who has also passed the impugned order in the instant case, Ketan Parekh, his brother Kartik K. Parekh and their investment companies were debarred from buying, selling or dealing in securities in any manner directly or indirectly and were also debarred from association in the securities market for a period of 14 years. That order was upheld by this Tribunal on 14.7.2006. If the appellant, which is a Ketan Parekh entity and is controlled by him, is allowed to continue to operate as a stock broker in the securities market then we would be allowing Ketan Parekh to operate in the market which would render the order dated 12.12.2003 meaningless. Since Ketan Parekh has been debarred from accessing the capital market it is necessary that all his entities must also be debarred or else the order debarring him would become redundant. We are, therefore, in agreement with the findings recorded by the Board in this regard.

No other point was raised.

In the result, the appeals fail and the same stand dismissed leaving the parties to bear their own costs.

Justice N.K. Sodhi
Presiding Officer

R.N. Bhardwaj
Member

BBN

