

**BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI**

Appeal No.105 of 2007

Date of decision:29.9.2008

1. Ramod Kumar Agrawal (HUF)
2. Sumitra Devi Agrawal
3. Rahul Kumar Agrawal Appellants

Versus

Adjudicating Officer,
Securities and Exchange Board of India Respondent

Mr. Vinay Chauhan Advocate for Appellants.

Dr. Poornima Advani Advocate with Ms. Sejal Shah Advocate for the Respondent.

Coram: Justice N.K. Sodhi, Presiding Officer
Arun Bhargava, Member
Utpal Bhattacharya, Member

Per: Utpal Bhattacharya, Member

This appeal has been filed against the order dated 29.3.2007 passed by the adjudicating officer, Securities and Exchange Board of India (the Board for short) imposing a penalty of Rs.25 lacs collectively on the Appellants Ramod Kumar Agrawal (HUF) – Appellant no.1, Sumitra Devi Agrawal -Appellant no.2 and wife of Appellant no.1 and Rahul Kumar Agrawal - Appellant no.3 and son of Appellant no.1. The penalty has been imposed under section 15 HA of the Securities and Exchange Board of India Act, 1992 for violation of Regulation 4(2) (a) of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations 2003 (hereinafter referred to as FUTP Regulations).

2. At the outset, we may note the salient facts of the case. Sometime in July 2005 one Bimal Kumar Agrawal (Bimal for short) who is the younger brother of Appellant no.1 and the Director of Rajat Share and Stock Brokers Pvt. Ltd. (Rajat for short), a member broker of the Magadh Stock Exchange Association (MSEA for short) where trading had been suspended by the Board, informed Appellant no.1 that trading on MSEA was going to commence shortly and the Appellants could trade through him

on MSEA. It is an admitted fact that the Appellants, who are based in Mumbai, normally trade in the securities market through a member broker of the Bombay Stock Exchange. On the request of Bimal, they became his clients and traded on MSEA through Bimal between 3.8.2005 and 12.8.2005. MSEA, which was a registered stock exchange, still did not have the permission of the Board to allow trading on its floor and the latter stopped such trading on the floor of MSEA after 12.8.2005. It is the Board's case that during August, 2005 the Appellants traded in 19 scrips on MSEA though none of the scrips were listed there and besides that, the transactions were not genuine as they were reversed between the Appellants on one side and one other particular trader on the other side through their respective brokers. These transactions, however, constituted a small percentage of the total transactions on MSEA in August 2005. An overwhelming percentage of such transactions pertained to the scrip of a company called Bhoruka Financial Services Limited (BFSL). The shares of BFSL were listed only on the Bangalore Stock Exchange but those were traded on the floor of MSEA under the permitted category between 1.8.2005 and 12.8.2005 when 98.73% of BFSL's equity owned by its promoters were sold to a single purchaser for Rs.89.28 crores. These transactions in BFSL's equity were illegal according to the Board since MSEA was not authorized to allow any trading on its floor but it did permit the trading in BFSL's equity under the permitted category. In its show cause notice to the Appellants, the Board alleged that the trades of the Appellants, besides being artificial in nature, were actually executed to create a false and misleading appearance of trading in MSEA in order to give a colour of authenticity to the illegal trades in BFSL's equity which, according to the Board was the real reason why the MSEA management allowed trading on MSEA though it was not authorized to do so.

3. The learned counsel for the Appellants stated that they readily agreed to start trading on MSEA since Bimal had offered to charge lower brokerage and also promised to allow day trading. Admittedly, the Appellants traded on MSEA on the say-so of the broker Rajat whose Director Bimal is the younger brother of Appellant no 1. The learned counsel for the respondent Board pointed out that whereas on MSEA their trades were all reversed as is normally done by day traders, the Appellants were

admittedly long term investors and normally did not engage in day trading. This uncharacteristic trading, according to the learned counsel, was done at the behest of broker Rajat so that an impression of a larger volume of trading could be created. According to the learned counsel, the fact that during the period in question all the trades on MSEA other than those in the equity of BFSL were executed by only two brokers and they had only one client each, can only lead to the conclusion that all these trades were reverse trades and were only meant to generate volumes.

4. In order to arrive at a conclusion as to whether the Appellants could be held responsible for executing these trades, it is necessary to consider the backdrop in which such trades were executed. It is clear from the material available on record that trading on MSEA, though not permitted by the Board, had been organized only for the purpose of sale of the shares of BFSL by its promoters. Such unauthorized trade could only be organized by persons who had authority over the management of MSEA and could also ensure smooth operation of the screen based trading system of the exchange. The Officiating Executive Director of MSEA and Bimal, the Director of Rajat and a member of the Council of Management of MSEA, were instrumental in organizing the trades on MSEA in August 2005. Of the trades executed on MSEA during that period, those involving shares of BFSL were clearly genuine in nature where ownership of the shares actually passed from the promoters of BFSL to the purchaser. The trades executed by the Appellants were, however, of a different nature. As brought out in the show cause notice issued to the Appellants by the Board, every single trade executed by the former, with the exception of only a few shares of ACC, were actually reversed and the net position of the Appellants in 18 out of 19 scrips in which they traded was nil. We, therefore, agree with the learned counsel for the Board that these trades were really meant to create an impression that not BFSL shares alone but many other scrips were trading on MSEA and such trading was normal and legal. If the Appellants knew at the time of executing the trades that those were reverse trades, then obviously they committed a serious wrong which attracts penalty under regulation 4(2)(a) of the FUTP Regulations which reads as under:

4. Prohibition of manipulative, fraudulent and unfair trade practices

(1).....

.....

(2) Dealing in securities shall be deemed to be a fraudulent or an unfair trade practice if it involves fraud and may include all or any of the following, namely:-

(a) indulging in an act which creates false or misleading appearance of trading in the securities market;

.....

.....”

5. Considering the facts and circumstances of the case, we do not think that the Appellants executed the impugned trades knowingly. A unique feature of the screen-based trading system is that it maintains anonymity of the buyer and the seller and it is not possible for either of them to know at the time of the execution of the trade as to who the counterparty is. This fact can be discovered by the Board or the exchange on an enquiry after the execution of the trade. The trades of the Appellants in this case had to necessarily reverse because when they traded on MSEA on the asking of Bimal, there were only two traders – one on either side and this knowledge cannot be attributed to the Appellants particularly in the absence of any material that could lead one to believe otherwise.

6. In the result, we do not agree with the Board that the Appellants can be held guilty of executing any fraudulent or unfair trade. Accordingly, the appeal is allowed and the impugned order set aside with no order as to costs.

Sd/-
Justice N.K. Sodhi
Presiding Officer

Sd/-
Arun Bhargava
Member

Sd/-
Utpal Bhattacharya
Member

