BEFORE THE ADJUDICATING OFFICER

SECURITIES AND EXCHANGE BOARD OF INDIA

[ADJUDICATION ORDER NO.: - SD/AO/94/2010]

UNDER SECTION 15-I OF SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 READ WITH RULE 5 OF SEBI (PROCEDURE FOR HOLDING INQUIRY AND IMPOSING PENALTIES BY ADJUDICATING OFFICER) RULES, 1995

In respect of

Shri Sachin Patil
PAN: Not Available

In the matter of
M/s. Vijay Textiles Ltd.

FACTS OF THE CASE IN BRIEF

1. The Securities and Exchange Board of India (hereinafter referred to as 'SEBI') has investigated into the dealings in the scrip of Vijay Textiles Limited (hereinafter referred to as '**VTL**') for the period of November 1, 2004 to March 11, 2005.

2. The role of the brokers and their clients who had traded in the scrip of VTL were scrutinized. It was alleged that through collusion with the brokers and other clients, certain entities transacted in the shares of VTL in such a manner that led to creation of artificial volumes in the scrip and distorted market equilibrium leading to wide fluctuation in the price of the scrip

which did not have any correlation with the performance of the company.

3. It was alleged that one of the entities, viz., Shri Sachin Patil(hereinafter referred to as **"Noticee"**), client of M/s DPS Shares and Stock Pvt. Ltd. violated the provisions of regulations 4 (1), 4 (2) (a),(b) and (g) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Markets) Regulations, 2003 (hereinafter referred to as **"PFUTP Regulations"**) and therefore, liable for monetary penalty under section 15HA of Securities and Exchange Board of India Act, 1992 (hereinafter referred to as "**SEBI Act**").

APPOINTMENT OF ADJUDICATING OFFICER

4. Ms. Babita Rayudu was appointed as the Adjudicating Officer vide order of SEBI dated August 31, 2007 under section 15-I of the Act r/w rule 3 of SEBI (Procedure for holding Inquiry and Imposing Penalty by Adjudicating Officer) Rules, 1995 (hereinafter referred to as the Adjudicating Rules) to inquire into and adjudge under Section 15HA of the Act, the alleged violation of the provisions of regulations 4 (1), 4 (2) (a), (b) and (g) of the PFUTP Regulations.

5. Consequently, the then Adjudicating Officer was sent on deputation and thereafter the undersigned was appointed as the Adjudicating Officer in the instant matter vide SEBI order dated November 23, 2007.

SHOW CAUSE NOTICE/ REPLY

6. A show cause notice in terms of the provisions of Rule 4(1) of the Adjudicating Rules was issued to the Noticee on May 28,

2008 seeking reply of the Noticee as to why an inquiry should not be held against the Noticee in respect of the violations alleged to have been committed by him. The said notice has been duly delivered at the address of the Noticee and the acknowledgment for the same is on record.

7. It is noted that noticee has not filed any reply in response to the said show cause notice. As a reminder the said show cause notice was affixed at the last known address of the Noticee. However, the Noticee did not respond to the same. On considering the facts of the case, it was decided to conduct an inquiry in the matter and the noticee was granted an opportunity of personal hearing and accordingly was advised to attend the hearing on July 22, 2010. The said notice of hearing was duly affixed at the last known address of the Noticee. As the Noticee has failed to respond to the abovementioned notices, it can be assumed that he is not willing to cooperate with the adjudication proceedings and accordingly the matter has been proceeded with based on material on record.

8. As the noticee has not put up any defence or challenged the show cause notice, it can be assumed that the charges levelled in the show cause notice has been accepted by the Noticee. This is in accordance with the principle laid by Hon'ble Securities Appellate Tribunal in the matter of ***Classic Credit Ltd. v. SEBI*** **[2007] 76 SCL 51 (SAT - MUM.) wherein it was inter-alia held that**

"…The appellants did not file any reply to the second show-cause notice. This being so, it has to be presumed that the charges alleged against them in the show-cause notice were admitted by them".

However, in order to pass a speaking order, the undersigned is going to analyse the evidence and allegations against the Noticee.

CONSIDERATION OF EVIDENCE AND FINDINGS

9. The allegation against the noticee is that he has entered into circular trading with certain other brokers and clients while trading in the scrip of VTL and thus created artificial volume and influenced the price of the scrip.

10. It is observed from the Investigation Report (**"IR"**) that Noticee has executed 1352 trades resulting from 249 buy orders and 254 sell orders leading to a total traded quantity of 6,13,650 shares during the first period of investigation. The Noticee traded for 12 days in a circular pattern during the first period. The total trading done by the Noticee in circular pattern is 2,55,400 shares. The **Table I** below shows the details of total trading done by the Noticee in circular pattern.

Name of the Broker & Broker code	Name of the major client & Client/s Code	No of Days Traded During the Period / No of Days Done Circular Trading	Buy Quantity (Circular)	% of market traded Quantity	Sell Quantity (Circular)	% of market traded Qty.	Gross Circular traded Qty. (% to total trading of the broker)	% of gross market traded Qty.
Adolf Pinto	**Sunil Jhaveri**	12/12	142250	3.34	161400	3.79	303650	3.57
Pawankumar Chaudhary	**Own account**	13/12	169500	3.98	137550	3.23	307050	3.60
DPS Shares and Securities Pvt. Ltd.	**Sachin Patil**	12/12	139050	3.27	116350	2.73	255400	3.00
S P J Stock Brokers Pvt. Ltd.	**Own account**	9/9	47000	1.10	65350	1.53	112350	1.32
Vijay Bhagwandas Shah	**Own account**	18/12	115850	2.72	133000	3.12	248850	2.92
TOTAL			613650	14.41	613650	14.41	1227300	14.41
Market Volume on BSE during the Period I			4258676		4258676		8517352	

11. Thus it can be seen that the Noticee was clearly dealing in a manner so as to defy the normal price discovery mechanism of a stock exchange. The Noticee has dealt in such huge volume that it can be concluded that such trading could not have been due to coincidence. Thus, it is very clear that that the Noticee had a prior meeting of minds with the other connected entities with whom he was trading.

12. The Hon'ble SAT in the case of Gautam Jhaveri v. AO, SEBI, appeal No. 131 of 2006, Decided on August 23, 2007 has held that

*"…**2.** We have heard the learned counsel for the parties. There is on record Table A referred to in the impugned order which contains the details of the trades executed by the appellant and Nrupesh Shah through their respective brokers. It is clear from this chart that on 27-5-2003 the appellant sold 5000 shares through Grishma Securities Pvt. Ltd. at the rate of Rs. 88.30 and the purchaser was Nrupesh Shah who purchased the same through his broker ISE Securities and Services Ltd. of which Anil Mistry is a member. The buy order was placed at 13:07:31 hours and the sell order was punched into the system at 13:07:32 hours. The price of the security punched into the system both by the buyer and seller was the same, the quantity of the shares to be sold was also the same and the time at which the two orders were punched in is almost the same. There is a time differential of only one second. **We have gone through this chart in great detail and find that as many as 327 trades were executed between the appellant and Nrupesh Shah which exactly matched in terms of price, quantity and the time. This could not have been a co-incidence. There was obviously a prior meeting of their minds and it was as a result of their design that the matching orders were punched into the system so that the trades could be executed. It is clear from the chart that when the appellant was the seller of the shares Nrupesh Shah purchased them and when the latter was***

selling them the appellant was the purchaser. In a screen based trading system that is followed in the stock exchanges, it is not possible that such large number of trades could match without the two clients executing a pre-decided plan. A unique feature of the trading system is that trading takes place between the unknowns who never get to meet and that the seller sells his shares without being bothered as to who the purchaser is. Similarly, the purchaser is not expected to be concerned as to the person from whom he purchases the shares. Again, another feature of the stock exchange is that even amongst the unknowns, trading takes place at the price which is determined by the price discovery mechanism of the exchange which is based on the principle of free forces of demand and supply. When two traders join hands and punch into the system their orders with a predetermined price for the same quantity at almost the same time, they obviously interfere with the true price discovery mechanism of the exchange. This is, indeed, a serious market irregularity. *The trades were circular because the shares moved from the appellant to Nrupesh Shah and back without the intention of transferring the beneficial ownership therein. Having regard to the number of matching trades we have no hesitation in upholding the finding of the adjudicating officer which we hereby do."*

13. Thus, it is very clear that the Noticee has prior understanding with the other entities and the number of trades is a clear proof of the same.

14. It is thus alleged that the Noticee violated regulations 4 (1), 4 (2) (a), (b), (e) and (g) of PFUTP Regulations which interalia states as follows:

"4. <u>Prohibition of manipulative, fraudulent and unfair trade practices</u>

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

(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;
> (b) dealing in a security not intended to effect transfer of beneficial ownership but intended to operate only as a device to inflate, depress or cause fluctuations in the price of such security for wrongful gain or avoidance of loss;
> …
> (g) entering into a transaction in securities without intention of performing it or without intention of change of ownership of such security; "

15. From the observations stated above and the material on record it is clear that the Noticee had traded substantially in the scrip of VTL and the Noticee was acting in collusion with other entities of the group for the common objective of creation of artificial volume. It is further observed that the Noticee along with other related entities executed a huge amount of circular trades and has created artificial volume in market and has thus hampered the price discovery of the scrip of VTL. Volume of a scrip is one of the important criterion on which investment decisions are taken by many small investors. If the volume in a scrip is high, it is likely to garner more investor interest and consequently more investors would be investing in that scrip. However, when the volume created is artificial then it will disturb the market

equilibrium and consequently many gullible investors end up loosing money.

16. The Hon'ble SAT in the matter of *Ketan Parekh v. Securities and Exchange Board of India*, *Appeal no. 2 of 2004,* has held that

"…*Any transaction executed with the intention to defeat the market mechanism whether negotiated or not would be illegal. Whether a transaction has been executed with the intention to manipulate the market or defeat its mechanism will depend upon the intention of the parties which could be inferred from the attending circumstances because direct evidence in such cases may not be available.* ***The nature of the transaction executed, the frequency with which such transactions are undertaken, the value of the transactions, whether they involve circular trading and whether there is real change of beneficial ownership, the conditions then prevailing in the market are some of the factors which go to show the intention of the parties****. This list of factors, in the very nature of things, cannot be exhaustive. Any one factor may or may not be decisive and it is from the cumulative effect of these that an inference will have to be drawn."*

17. It is thus clear that the trading of the Noticee was clearly dubious and was with a premeditated intent. The Noticee's is an important part of the group and he has made a dominant contribution during the first period. It is thus very clear that the Noticee was a part of the game plan and has been involved in manipulative trading.

18. In view of the abovementioned observations and findings and all the material on record, I am of the opinion that the Noticee had violated Regulation 4 (1) and 4 (2) (a), (b) and (g) of the PFUTP Regulations which warrants monetary penalty under Section 15HA of the SEBI Act.

19. In view of the foregoing, I am convinced that it is a fit case to impose monetary penalty under section 15HA of the SEBI Act. In view of the above, the next issue for consideration is as to what would be the monetary penalty that can be imposed on the Noticee for the violation of abovementioned provisions of the PFUTP Regulations.

20. The Hon'ble Supreme Court of India in the matter of ***SEBI v. Shri Ram Mutual Fund*** [2006] 68 SCL 216(SC) interalia held that "once the violation of statutory regulations is established, imposition of penalty becomes *sine qua non* of violation and the intention of parties committing such violation becomes totally irrelevant. Thus, as the violation of statutory obligations by the Acquirers has been established, I hold that they are liable for monetary penalty."

21. The provisions of section 15HA of the SEBI Act as prevailing at the relevant time are reproduced hereunder :

    *"**Penalty for fraudulent and unfair trade practices.***
    15HA. If any person indulges in fraudulent and unfair trade practices relating to securities, he shall be liable to a penalty of twenty-five crore rupees or three times the amount of profits made out of such practices, whichever is higher."

22. While imposing monetary penalty it is important to consider the factors stipulated in section 15J of SEBI Act, which reads as under:

"15J - Factors to be taken into account by the adjudicating officer

While adjudging quantum of penalty under section 15-I, the adjudicating officer shall have due regard to the following factors, namely:-

(a) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default;

(b) the amount of loss caused to an investor or group of investors as a result of the default;

(c) the repetitive nature of the default."

23. It is noted from the details available on record that the noticee had executed substantial trades in the scrip. Further, the noticee is stated to have bought a large number of shares of a company which has shown a dismal performance and does not have a good track record. Moreover, the Noticee has acted in collusion with other entities and has tried to give a false impression of trading to the innocent investors and has thus created artificial volume and has also influenced the price of the scrip. Such type of trading has definitely caused a loss to the investors and has left them in a lurch after these connected entities rig the price and exit the scrip by off-loading their shares. However, the amount of disproportionate gain made by the Noticee or the loss caused to the investors cannot be computed. Further, the Noticee has been a repetitive defaulter and has been penalized earlier in various matters.

24. In view of the above observations, findings and material on record I conclude that the allegation of violation of Regulation 4

(1) and 4 (2) (a),(b) and (g) of the PFUTP Regulations against the Noticee stands proved.

ORDER

25. In view of the above, after considering all the facts and circumstances of the case and exercising the powers conferred upon me U/s. 15-I(2) of the Act, I hereby impose a monetary penalty of Rs. 5,00,000/- (Rupees Five Lakhs only) on the Noticee. In the facts and circumstances of the case, I am of the view that the said penalty is commensurate with the violation committed by Shri Sachin Patil.

26. The penalty shall be paid by way of demand draft drawn in favour of "SEBI – Penalties Remittable to Government of India" payable at Mumbai within 45 days of receipt of this order. The said demand draft shall be forwarded to Deputy General Manager, Investigation Department (ID8), Securities and Exchange Board of India, Plot No. C4-A, 'G' Block, Bandra Kurla Complex, Bandra (E), Mumbai – 400 051.

27. In terms of the provisions of Rule 6 of the SEBI (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules 1995, copies of this order are sent to Shri Sachin Patil and also to Securities and Exchange Board of India.

Date: July 30, 2010	**SANDEEP DEORE**
Place: Mumbai	**ADJUDICATING OFFICER**