

## SECURITIES AND EXCHANGE BOARD OF INDIA

**ORDER UNDER REGULATION 13 (4) READ WITH REGULATION 13 (6) OF SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002****IN THE MATTER OF M/S SAMKIT SHARES AND STOCK BROKERS PRIVATE LIMITED**

- 1.0 M/s Samkit Shares and Stock Brokers Private Limited (hereinafter referred to as 'the said broker') is registered with Securities and Exchange Board of India (hereinafter referred to as 'SEBI') as a broker - SEBI Registration no.INB 021050332 and is a member of the Stock Exchange, Ahmedabad (hereinafter referred to as 'the ASE').
- 1.1 During inspection of the books of account, records and other documents of the said broker undertaken by SEBI during January, 2001 under Regulation 19(1) of the SEBI (Stock Brokers and Sub Brokers) Regulations, 1992 (hereinafter referred to as 'the said regulations') certain violations were observed. Findings of the inspection were forwarded to the said broker for its comments.
- 2.0 After considering the inspection report and the comments of the said broker thereon, it was decided to conduct an enquiry into the affairs of the said broker, in terms of Regulation 28 of the said regulations. Accordingly, vide order dated June 18, 2002, Shri. S.V. Krishnamohan was appointed as an enquiry officer for holding an enquiry into the contraventions by the said broker of the provisions of rule 4 (b) and (d) of the SEBI (Stock Brokers and Sub-Brokers) Rules, 1992 (the said rules) regulation 10 (1) and clauses A(5) and (B)(1) of the Code of Conduct as specified in Schedule II read with regulation 7 of the said regulations, directives issued by SEBI as mentioned in the said order and Bye-laws, Rules and Regulations of ASE and directives issued by ASE from time to time.
- 2.1 The enquiry officer issued a show cause notice dated July 26, 2002 to the said broker under regulation 28 (2) of the said regulations. After considering the reply of the said broker and submissions made on its behalf during personal hearing before him, the enquiry officer submitted the enquiry report dated October 31, 2002.
- 2.2 The enquiry officer, in his report recorded his findings as under –
- i. In view of the payment of turnover fees along with interest as certified by the Chartered Accountant (Moulik M. Shah) as submitted by the said broker, the charge of violation of rule 4 (d) of the said rules and regulation 10 (1) of the said regulations may be viewed leniently although the payment is made subsequent to the inspection.
  - ii. Regarding delay in transfer of securities from the brokers pool account to the beneficiaries' account as cited in 15 instances quoted in the show cause notice and the enquiry report it was observed that the securities were not transferred for periods ranging from 16 days to 5 months. The said broker had submitted that the clients themselves had authorized it to retain the shares in the pool account so that the shares could be sold in the near future. The said broker had filed the authorization letters of the clients in this regard before the Enquiry Officer. The Enquiry Officer has noted that in case of one Shri Chandrakant Patel in respect of 336 shares of Global Tele Systems the delay is not such satisfactorily explained since the purported authorization letter is not signed. In this case the said broker has violated clause B (1) of the Code of Conduct as specified in Schedule II read with regulation 7 of the said regulations and SEBI circular no.SMDRP/POLICY/CIR/11-1999 dated 7.5.99.
  - iii. Regarding irregularities in the contract notes, said broker had explained satisfactorily to the Enquiry Officer which have been accepted by the Enquiry Officer. Regarding not maintaining clients agreements, the Enquiry Officer has given benefit of doubt to the said broker
  - iv. Regarding non segregation of clients and own bank accounts and deposit of clients fund into the general account, the Enquiry Officer has found that the said broker has met certain office expenses from the clients account which is highly irregular and in violation of SEBI circular no.SMD/SED/CIR/93/23321 dated 18.11.93.
  - v. Regarding indulging in cross deals and negotiated deals, the Enquiry Officer has found that the said broker has violated SEBI circular no.SMDRP/POLICY/CIR-32/99 dated 14.9.99 in respect of 11 instances as cited in the Enquiry Report.
  - vi. The enquiry officer found that the said broker has dealt with M/s.Vora Consultancy who is not registered with SEBI as a sub-broker in violation of SEBI Circular SMD/POLICY/3-97 dated 31<sup>st</sup> March, 1997.
- 2.3 Since SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty), Regulations, 2002 (hereinafter referred to as 'the Enquiry Proceedings Regulations') commenced on 27.09.2002 the enquiry officer conducted the proceedings under the said Enquiry Proceedings Regulations. In view of the above facts and findings, the enquiry officer recommended that the certificate of registration of the said broker be suspended for a period of six months.
- 3.0 The enquiry report was considered and in terms of Regulation 13(2) of SEBI Enquiry Proceedings Regulations, a show cause notice no. SMD/DBA-I/Enq/AM/23770/2002 dated December 04, 2002, was issued to the said broker enclosing therewith a copy of the enquiry report calling upon it to show cause as to why the penalty as recommended by the enquiry officer should not be imposed upon it. It was also advised to reply to the same together with the documents if any, that it may choose to rely upon in support of its reply, within 15 days of the receipt of the same, failing which it would be presumed that it has no explanation to offer. The said broker was also advised to intimate its desire of personal hearing along with its reply.
- 4.0 The said broker vide letter dated December 14, 2002 submitted its reply. In its reply the said broker has reiterated its submissions made before the Enquiry Officer. Regarding charges of non payment of turnover fees, irregularities regarding contract notes and clients agreement etc. it has pointed out that the Enquiry Officer has accepted its submissions.

Regarding dealing with M/s.Vora Consultancy, an unregistered sub-broker it has submitted that the application for registration of the said M/s.Vora Consultancy was made to SEBI on 10.1.01 and it was granted registration subsequently by SEBI under Registration No.INS021000810/0210503. Regarding indulging in cross deals and not segregating the clients and his own bank accounts, it has submitted that during the relevant time the broking business was new to it and the rules were violated in ignorance and not intentionally. Further, it had stopped doing cross deals and segregated the clients account and its own account from the day they were pointed out as violations. Regarding the delay in delivery of securities from pool account in case of Chandrakant Patel, it has submitted that unsigned authorization letter of the client was submitted due to sheer mistake. It has enclosed the signed copy of the purported authorization letter of Chandrakant Patel dated 24.4.2000. It has pleaded that the penalty of suspension would be very harsh and requested to take a lenient view. It had also sought personal hearing in the matter.

- 5.0 An opportunity of personal hearing was given to the said broker on 27.02.2003. On the said date Mr. Prakash K. Shah of Ketan Rupani & Co., Chartered Accountants authorized by the said stock broker appeared and reiterated the earlier submissions of the said broker. He filed a written submission and made additional submissions not submitted before the Enquiry Officer earlier. The submissions are mainly regarding dealing with Vora Consultancy being an unregistered sub-broker, the segregation of clients and brokers account and payment of expenses from clients account. He submitted that prior to registration as sub-broker, M/s.Vora Consultancy has carried out transactions on its own account for itself. He has filed a letter dated 18.2.03 confirming the same. He submitted that the amounts received from the clients were in the nature of loan transactions and not for the purpose of trade and payment of Rs.1832/- from clients account towards expenses was withdrawn against the brokers own money lying in the clients account. He requested that in view of the submissions made a lenient view may be taken in the matter.

## 6.0 Findings –

- 6.1 I have considered the oral and written submissions made by and on behalf of the said broker, findings and recommendations of the enquiry officer as contained in the enquiry report and the relevant material available on record.

- 6.2 The issues in the matter and my findings thereon are as under -

### A) Delay in delivery of securities from the pool account to the beneficiaries' account

I find that the broker has sought to justify the delays in delivery of securities from pool account to beneficiaries' account which were ranging from 16 days to 5 months in 15 instances on the plea that the same were authorized by the clients. In case of Shri Chandrakant Patel in respect of 336 shares of Global Tele Systems, the purported authorization letter dated 24.4.2000 has been signed. However the said letter was not signed when it was submitted before the Enquiry Officer. It is clear that the signature has been taken afterwards. As per the circular dated 7.5.99 a member is required to deliver the shares to beneficiary account immediately after pay out and make the balance in the pool account nil within 15 days of pay-out. Such requirement cannot be waived or authorized by the client. The obligation is on the broker to make the balance in the pool account nil within 15 days of the pay-out. If the brokers are allowed to hold the shares such as for period over 16 days to 5 months, it would make mockery of a depository which is supposed to hold the demat shares. In this case the said broker has violated clause B (1) of the Code of Conduct as specified in Schedule II read with regulation 7 of the said regulations read with SEBI circular no.SMDRP/POLICY/CIR/11-1999 dated 7.5.99.

### B) Non segregation of clients account and own account and deposit of clients fund into the general account

I find that during the period under inspection, it was found that the said broker had deposited money received from clients directly into O/D A/c. No.120 maintained with Central Bank of India as General Account. During inspection following such instances were noted :-

| Sr. No. | Date     | Name                      | Amount    |
|---------|----------|---------------------------|-----------|
| 1.      | 09.04.99 | Jaya C. Shah              | 25000.00  |
| 2.      | 15.04.99 | S. R. Makwana             | 10000.00  |
| 3.      | 06.05.99 | Kamlesh Bhai Kalidas Shah | 2025.00   |
| 4.      | 14.05.99 | Kamal Investment          | 10000.00  |
| 5.      | 18.05.99 | Jigar C. Shah             | 10000.00  |
| 6.      | 24.05.99 | Kamlesh Bhai Kalidas Shah | 150000.00 |
| 7.      | 28.08.99 | Jaydeep Sharefin          | 100000.00 |

It is also observed that the said broker has paid its own expenses from clients account. The said broker had paid Rs.1,000/- towards office expenses on 3.5.2000 and Rs.832/- towards petrol expenses on 15.11.2000 from the client account no.938 maintained with Central Bank of India.

I find that before the Enquiry Officer and also in reply to the show cause notice dated 4.12.2002 the said broker had submitted that the rules were violated in ignorance and since the business was new. The segregation has been done when it was pointed out as violation. During hearing before me it is submitted that amount received was in the nature of loan transactions and not for the purpose of trade without submitting any proof in this regard. I find that this submission is an afterthought and not maintainable particularly in absence of any proof. It is also observed that the said broker has paid its own expenses from clients account. The submissions made during hearing that the amount of Rs.1832/- was withdrawn against the brokers own money lying in the clients account is also not acceptable. It is not clear as to on what basis this amount of broker as submitted was lying in clients account. No proof or evidence has been submitted in this regard. It may be mentioned that by the circular no. SMD/SED/CIR/93/23321 dated November 18, 1993 it has been made compulsory for all the brokers to keep the money of the client in a separate account and their own money in a separate account. Further, it has been stipulated that no payment for transactions in which the member broker is taking a position as a principal will be allowed to be made from the clients account. The circumstances under which transfer from clients account to brokers account is allowed are enumerated in the said circular. The circular provides that the money required for

payment to or on behalf of clients or for or towards payment of a debt due to the broker from client or money drawn on clients authority or money in respect of which there is a liability of client to the broker. The object behind this norm is that the clients' money is used mainly for the purposes of meeting out the clients liabilities and to prevent misuse of clients' money. I note that vide circular no. SMD/MDP/CIR/043/96 dated August 5, 1996, it has been directed that in case of deficiency in having separate bank account for clients but not segregating clients funds from the own funds by the brokers, a serious view will be taken.

By the circular no. SMD/SED/CIR/93/23321 dated November 18, 1993 all the stock exchanges have been directed to make necessary provisions in their bye-laws and regulations for the purpose of giving effect to the norms contained in the said circular. I find that the ASE bye-laws 226(d) provide for the said norms of regulation of transactions between clients and brokers. The said bye-laws provide that it is compulsory for every member to keep the money of the constituents in a separate bank account and their own money in a separate bank account. It is further provided that every member who holds or receives money on account of a constituent shall forthwith pay such money to the client account. It is further prohibited that no money shall be drawn from the constituents account other than the money required for payment to or on behalf of the constituents or for payment of a debt due to the member from the constituent etc.

I observe that the said broker has not been able to establish that it has not misused the clients account and find that the said broker has violated the requirements as stipulated in SEBI circular no. SMD/SED/CIR/93/23321 dated 18.11.93 and bye-laws 226(d) of the ASE. In this regard, I find that the said broker has contravened the condition of certificate as provided in rule 4(b) of the said rules which contemplates that the certificate of registration to a stock broker is granted subject to the condition inter alia that he shall abide by the rules, regulations and bye-laws of the stock exchange of which he is a member.

### **c) Indulging in off the market transactions / cross deals –**

I find that the said broker has admitted that it has conducted off the market deals in 11 transactions as cited in the Enquiry Report as recorded by the enquiry officer. The said broker has submitted that it had stopped such transactions after the same was pointed out as violation. I find that the said broker has carried out such transactions during the period under inspection which are in violation of SEBI circular dated 14.09.1999. By the said circular it was required that all negotiated deals shall be executed only on the screens of the exchanges in the price and order matching mechanism of the exchanges just like any other normal trade. Such transaction tempers with price discovery mechanism and transparency in price discovery process. I agree with the findings of the Enquiry Officer as recorded in the Enquiry Report. The submission that the ASE in its further inspection has not observed such lapses cannot exonerate the said broker for the violations which have been committed during the period of inspection.

### **d) Dealing with unregistered sub-brokers.**

I agree with the findings of the enquiry officer in this regard. I find that the application of M/s.Vora Consultancy was sent to SEBI on 10.1.2001 and registration was granted on 23.3.2001. The transactions were done before the registration was granted to the said Vora Consultancy. Therefore, the submissions of the said broker are not tenable and are rejected. Vide circular No. SMD/POLICY/CIRCULAR/3-97 dated March 31, 1997 it has been directed that no broker shall deal with a person who is acting as a sub broker unless he is registered with SEBI. It shall be the responsibility of the broker to ensure that his clients are not acting in the capacity of a sub-broker unless he is registered with SEBI as a sub broker or he is recognized by the stock exchange as a remiser. I find that the said broker has violated the mandatory requirements of SEBI circular.

- 6.3 The submission that the violation is technical and due to ignorance does not in any way affect the fact that there is a violation. It is the statutory requirement prescribed under the said regulations and every stock broker is under obligation to comply with it a condition for grant of the certificate of registration in terms of rule 4 (b) of the SEBI (Stock Brokers and Sub-Brokers) Rules, 1992. It is for the safety and integrity of the market and proper regulation of the stock broker. These requirements are required to be complied with compulsorily. I find that as specified in clause A of the Code of Conduct for stock brokers as specified in Schedule II of the said Regulations, it is the duty of every stock broker to exercise due care and skill and diligence in the conduct of all his business.
- 6.4 In view of the above observations I find that the said broker is guilty of having violated the provisions of clauses A (5) and B(1), of the Code of Conduct as specified in Schedule II read with Regulation 7 of the Regulations and Rule 4(b) of the SEBI (Stock Brokers and Sub-brokers) Rules, 1992 and SEBI directives contained in the circulars as found hereinabove. In view of the same, the said broker is liable for action under regulation 13 (1) (b) of the Enquiry Proceedings Regulations.
- 6.5 Under section 11 of the SEBI Act, SEBI can take measures to protect the interests of investors and to regulate the securities market inter alia by registering and regulating the working of stock brokers. The directives contained in the SEBI circulars are the measures for regulating the working of the stock brokers. Further, the Code of Conduct specified in Schedule II of the said regulations also provides for the minimum standards for the working of the stock brokers. If the regulatory requirements are violated by the stock brokers on the ground that the violations are technical, the measures taken by SEBI for regulation of the stock brokers would be rendered nugatory and the regulatory function would be jeopardized. These requirements of segregation of clients fund with own funds, prohibition of cross deals, dealing with unregistered intermediaries etc are the requirements which SEBI has put in place for the purpose of investor protection and to remove certain mala fide practices. These cannot be viewed as technical violation.
- 6.6 It is to be noted that indulgence of the said broker in the transactions which are prohibited can not be allowed on the ground of any technicality or otherwise especially when such transactions are likely to have a detrimental effect on regulation of the securities market. Further, every stock broker is under obligation to comply with the provisions of the Act and the Rules and Regulations made thereunder as also the circulars and guidelines issued by the Board from time to time. It is also imperative that all the members of the stock Exchange shall adhere to the bye-laws of the Exchange.

- 6.7 Regulation 7 of the said Regulations provides that the stock broker holding the certificate shall at all times abide by the Code of Conduct as specified in Schedule II. Further, Clause A (5) of Schedule II provides that a stock broker shall abide by all the provisions of the Act and the Rules, Regulations issued by the Government, the Board and the Stock Exchange from time to time as may be applicable to him.
- 7.0 I find that the said broker has committed violations as observed above and has not taken due care and diligence in observance and compliance of the statutory requirement in conduct of its business as a stock broker. I find that the said broker has violated the condition of registration specified in rule 4 (b) of the SEBI (Stock Brokers and Sub-brokers) Rules, 1992. I find that the penalty as recommended by the enquiry officer may be reasonable in terms of regulation 13 (1) (b) (ii) read with regulation 13 (6) (b) of the Enquiry Regulations. Looking into the violations committed by the said broker, I am satisfied that it is necessary to secure the proper management of the stock broker and also in the interest of the securities market that a penalty of suspension of certificate of registration for a period of six months is reasonable. Therefore, in exercise of the powers conferred upon me by virtue of sub section (3) of section 4 of the Securities and Exchange Board of India Act, 1992 read with regulations 13 (4) and 13 (6) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 I hereby order that the certificate of M/s Samkit Shares and Stock Brokers Private Limited - SEBI Registration no. INB 021050332, a member of the Stock Exchange of India, Ahmedabad be suspended for a period of six months.

7.1 This order shall come into effect after three weeks from the date of this order.

**DATE : April 10, 2003**

**PLACE: MUMBAI**

**G. N. BAJPAI**

**CHAIRMAN**

**SECURITIES AND EXCHANGE BOARD OF INDIA**