

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 SUMEDHA FISCAL SERVICES LTD.**

1.0M/s.Sumedha Fiscal Services Ltd. (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 231075830 and is a member of the National Stock Exchange of India Limited (hereinafter referred to as 'the NSE').

1.1During inspection of the books of account, records and other documents of the said broker undertaken by SEBI from 7th to 10th November, 2000, under Regulation 19(1) of the SEBI(Stock Brokers and Sub Brokers) Regulations, 1992(hereinafter referred to as 'the said Regulations') following violations were observed :-

- order book, sauda book, Margin Deposit Book and document register were not maintained by the said broker.
- contract notes were not issued to two clients namely, Alok Khetan and Sureka Investments.
- Client agreement form not properly filled up.
- The said broker has delayed payments to the clients.
- The said broker has delayed transfer of securities from pool account to client's account.
- The said broker had dealt with unregistered sub-brokers.
- The said broker has been carrying on business other than that of the securities business, i.e. Leasing business.
- Non segregation of client's funds and own funds.
- Margins have not been collected from clients.

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 29.04.2002 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 the rules, regulations and directives as mentioned in the said order.

2.1The enquiry officer issued a show cause notice dated 17.07.2002 to the said broker under regulation 28 (2) of the said Regulations. The enquiry proceedings were conducted as per the procedure laid down in the said Regulations. In terms of Regulation 28(4), the member was given a fair and reasonable opportunity of hearing to enable him to make submissions in support of his reply.

2.2After 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 November 25, 2002. Since SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty), Regulations, 2002 (hereinafter referred to as 'Enquiry Proceedings Regulations') commenced on 27.09.2002, the enquiry officer has recommended the penalty under the said Enquiry Proceedings Regulations. In view of the facts and findings as recorded in the enquiry report, the enquiry officer, in terms of Regulation 13 (1) b) of Enquiry Proceedings Regulations, recommended that the certificate of registration of the said broker be suspended for a period of four months.

2.3 In the enquiry report the enquiry officer has recorded his findings as under-

i) Non maintenance of order book

Although it is stated that all records of the transactions including the order number generated by the stock exchange system are being maintained electronically, maintenance of order book is a mandatory requirement and non compliance of the same is in violation of SEBI Circular SMD/POLICY/IECG/1-97 dated 11/2/1997.

ii) Non maintenance of sauda book

Even though the trades of Alok Khetan operating from a terminal are duly reflected on a said broker's counter and confirmed on daily basis, nevertheless, it does not obviate the need to maintain the sauda book which is a statutory requirement. Non maintenance of the same is not in compliance with Rule 15(1) Securities Contracts (Regulation) Rules, 1957[SC(R)]and Regulation 17(1) of the said Regulations. The practice of the said broker in routing certain transaction through miscellaneous accounts and entering the client details at the end of the day is irregular. The explanation of the said broker that this practice was adopted to save paper work is not satisfactory. However, taking into account the total volume of transactions which is Rs.10 lakhs annually as against the total turnover of 1,95,800 lakhs i.e. .05% of the turnover, the matter may not be viewed seriously.

iii) Non issuance of contract notes to two clients

Contract note is a primary document evidencing the contract between the parties. In the absence of a proper contract note, the client does not have any recourse in law to enforce the obligations arising out of the transaction. There would be difficulties in resolving the disputes in the absence of a valid contract note or for reference of dispute to the arbitration by the stock exchange. Even if the client has asked the said broker not to issue the contract note as claimed in the case of Alok Khetan, it is the duty of the said broker to maintain duplicate copies of the contract note containing the acknowledgement of the client and preserve the same for the prescribed period under the Regulations and show it to the inspecting authority. In view of the above, the explanation of the said broker in this regard is not satisfactory. Although it was claimed that settlement wise contract notes were issued in the case of Sureka Investments, no evidence was forthcoming in the enquiry proceedings in support of this contention. Even otherwise, this is not a substitute for issuance of regular and proper contract notes on daily basis. Both these

clients constitute for nearly 50% of the business of the said broker and non issuance of contract notes for these clients means that majority of the trades are not backed by contract notes which is highly irregular. It is, therefore, concluded that the said broker was not issuing the contract notes which is in violation of Rule 15(2) (b) of the SC(R)R and Regulation 17(1) (i) of the said Regulations. Similarly, routing of transactions through miscellaneous accounts and taking out the contract notes in the name of "miscellaneous account" and subsequently inserting the name of the client on the contract note manually is not a correct procedure.

iv) Non maintenance of margin deposit book

Although it was replied by the said broker that the margin payable was downloaded from the exchange system and maintained, this does not obviate the need to maintain a margin deposit book which is a statutory book to be maintained by the broker in terms of SC(R) R and Regulation 17(1) (k) of the said Regulations.

v) Non maintenance of document register

While it is true that with the advancement of electronic transfer of securities and the shares being held in electronic form which are fungible, the concept of distinctive number of shares is non-existent for such shares. However, for the shares which are still in the physical form, the distinctive numbers are relevant and are required to be entered in the document register. Non maintenance of the same would be in violation of Rule 15(1)(g) of SC(R) R and Regulation 17(1) (g) of the said Regulations.

vi) Client agreement form not properly filled up

As regards the charge that the client agreement forms were not properly maintained, the show cause notice cited the following deficiencies.

Sl.No.	Name of client	Deficiencies noticed in client agreement form	Deficiencies noticed in client registration forms
1.	Ashok Kumar Bong	NA	Photograph and proof of identity/residence missing
2.	Archana Ray	Signature of witness missing	N.A
3.	Saroj Bajaj	N.A.	Photograph and proof of identity/residence missing
4.	Sangeeta Parekh	Signature of witness missing, form not properly filled up	Proof of identity/residence missing
5.	Amal Krishna Kundu	Signature of client, member, witness missing	N.A.

In three instances (Ashok Kumar Bong, Archana Ray, Saroj Bajaj), the clients are stated to be non active and in one instance (Amal Krishna Kundu) the deficiency "was being rectified". In the case of Sangeeta Parekh, the explanation of the said broker has been found to be satisfactory in view of the details of her husband who is also a client of the said broker.

That the clients are not active does not obviate the need to maintain the client registration forms and client agreement forms in order. Infact, before registering a client, all the particulars of the clients are required to be obtained. This is a condition precedent for executing any transaction in securities on behalf of the clients.

Client identification is important since that makes it easier for the audit trail to identify the clients behind the transactions. Details like bank account, PAN number, introducer photograph, proof of residence etc would establish the credentials of the clients and would be relevant to determine whether the said broker had acted in good faith and without negligence before doing business for a client. Not filling up of the client registration forms properly or non maintenance of the same is in contravention of SEBI Circular SMD-1/ 23341 dated 18th November, 1993, SMD/POLICY/IECG/1-97 dated 11th February, 1997 and SMD/POLICY/Cir/5-97 dated 11th April, 1997.

vii) Delay in transfer of securities

The explanation of the said broker with regard to delay in transfer of securities beyond the permissible period of 15 days is found satisfactory and acceptable by the Enquiry Officer.

viii) Dealing with unregistered sub broker

As regards the allegation that the said broker was dealing with unregistered sub broker for his transaction with Sureka Investments, it was replied that initially he was a client who later on became their sub broker on 18/2/2002. It may be stated here that Sureka Investments is the second largest client of the said broker with a trading terminal in his premises at Bhubaneshwar.

It is observed that Sureka Investments had a turnover of Rs.1187661000 in the year 2000-2001 and Rs.729669440.70 as per the information submitted by the said broker himself. Having regard to the trading pattern and the volume of transactions, this client had with the said broker, it is highly probable that it was acting as unregistered sub broker for the said broker and in all probability dealing with ultimate clients. It is settled position of law that in an enquiry of this nature, strict rules of Evidence Act are not applicable and the charges need not be established beyond all reasonable doubts. It is sufficient if the preponderance of probability suggests towards commissioning of the misconduct.

In view of the above, there is high preponderance of probability that Sureka Investments was acting as sub broker. This view is fortified in view of the fact that Sureka Investments is the second largest "client" of the said broker with huge turnover as aforesaid.

ix) Delayed payments to clients

The explanation of the said broker with regard to the allegation of delayed payments in each of the twelve instances as mentioned in the Enquiry Report has been found to be satisfactory by the Enquiry Officer.

x) Carrying on business other than securities business, i.e. Leasing

business

The charge that the said broker had carried on leasing activity in violation of Rule 8(1) (f) and 8(3) (f) of SCR Rules, 1957 was not established during the enquiry.

xi) Non segregation of client's money and own funds.

The explanation of the said broker is not found satisfactory except to the extent of debiting of Bank Guarantee commission suo moto by the bank as mentioned in the Enquiry Report. The Enquiry Officer has observed that it is not known whether in the application for Bank Guarantee submitted to the bank, the said broker has instructed the bank to debit the Bank Guarantee issuance commission from this account. Therefore, the benefit of doubt is given to the said broker in respect of these two transactions. As regards the other transactions, the explanation of the said broker is not satisfactory. Cash withdrawals are made from the client's account and, office expenditure for purchase of computers etc. was debited to the client's account. Contributions to gratuity fund etc and payment of fees to the exchange for the derivatives segment were all met from the client's account which is highly irregular. These expenses are not client related and, therefore, cannot be said to be in conformity with the SEBI Circular SMD/SED/CIR/93/23321 dated 18th November, 1993 which clearly lays down as to what are the expenses that can be met from the client's account. Debiting of clients' account for the transactions which are not client related defeat the very purpose of maintaining clients' account separately. The amounts to the credit of clients' accounts are in the nature of trust and it is not in order for the said broker to meet other expenses which are not client related from such account. The funds in the client's account cannot be applied for any purpose other than what is permissible under SEBI Guidelines. The objective of opening and maintaining a separate account for the client's funds is to segregate and identify them separately and to prevent its misuse so that they are beyond the reach of the broker. The broker has met his office expenditure like computers, gratuity to staff etc. from this account, which is highly irregular. This is in violation of SEBI Circular SMD/SED/CIR/93/23321 dated 18th November, 1993.

xii) Non collection of margin from clients

As regards the allegation that the said broker was not collecting any upfront margins from the clients including from Alok Khetan and Sureka Investments who were his top most clients, the reply of the said broker that the margins were not collected as per the industry practice is not satisfactory. Margins are imposed by the exchange/ SEBI as an important tool for risk containment measures. Non collection of the same on the ground that clients were not paying margins or that it is an industry practice is highly irregular. It may be noted that the broker had not collected any margin from Alok Khetan and Sureka Investments who occupy the top two slots and contribute about 50% of the trading turnover with the said broker for the years 1999-2000 and 2000-2001.

Collection of margins as prescribed by SEBI guidelines is a risk containment measure which should be strictly adhered to. Non collection of margins are, therefore, in violation of SEBI Circular No. SMDRP/POLICY/CIR-07/2000 dated 4th February, 2000.

3.0 The enquiry report was considered and in terms of Regulation 13(2) of Enquiry Proceedings Regulations, a show cause notice no. SMD/DBA-I/Enq/AM/23836/2002 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. The said show cause notice was served through the NSE on the said broker. The said broker vide its letter dated December 26, 2002, confirmed that it had received the said show cause notice on December 13, 2002, from NSE and requested for additional time of two weeks for filing its reply. It also assured to file its reply not later than 14.01.03.

3.1 The said broker vide its letter dated 11.01.03 filed its reply. In the said reply the said broker has submitted *inter alia* as follows:-

a) each of the issues on the basis of which the major penalty has been recommended are minor, non material and unintentional irregularities;

b) no harm or damage has been caused to any investor, capital market, the regulators or any other concerned person. The technical irregularities have not resulted in any benefit or detriment to any person;

c) the errors and technical breaches are all back-office related and not front-office related;

d) the charge relating to alleged dealings with unregistered sub-brokers is contrary to facts;

e) the technical infirmities have been remedied and mistakes have been rectified;

f) at the time of alleged breaches the said Regulations were in place without amendments but the Enquiry Officer has recommended a penalty higher than what was contemplated in the said Regulations;

g) none of the ingredient of regulation 13 (6) of the Enquiry Proceedings Regulations have been brought forward by the Enquiry Officer;

h) since the orders are received on a real time basis from clients, it is normal to ensure compliance by creating the order book electronically and backing it up with the print out at the end of the day. These orders are entered in the NEAT trading screen directly and thereby automatically an order book is created. It is stated that NSE has done away with the mandatory requirement of maintenance of order book perhaps realizing practical difficulties in implementation of the rule;

i) It had terminals at four places with controlling counter being at Calcutta. Other terminals at Mumbai, India Exchange Place, Calcutta and Bhubaneswar. India Exchange counter was used to service only one group of client i.e. Alok Khetan and Bhubaneswar counter was for another client Sureka Investment. It had maintained sauda book for trades done by Alok Khetan and Sureka Investments at its respective offices at Calcutta and Bhubaneswar;

j) Except for serial number of contract note every other formal and substantive information was made available to the client. Mr.Alok Khetan was doing arbitrage business and was getting all details daily through net report, settlement bill, financial ledgers, daily position etc. and he had requested not to issue contract notes. The client himself has no grievance in this regard;

k)As per the business practice none of the clients were paying margins. Even though a margin deposit book was kept blank. It is now maintaining regular system of collection of margin and duly reflected in margin deposit book;

l) 'the document register is required to include particulars of shares and securities received and delivered. We have complied with the provision and have duly maintained such register. As other details connecting to Folio No., Share Certificate No. etc. are available in the Register. There is no provision of law requiring Distinctive Nos. to be maintained in the Document Register. Nevertheless, our document register contains particulars of bill no. which are filed in the same serial number as mentioned in the documents register. Hence, details of distinctive nos. are readily available to us through trail systems established by us;

m) while reiterating its submissions as recorded by the enquiry officer in the enquiry report, it has further submitted that the errors in respect of non maintenance of client agreement forms are clerical and technical and they do not merit any action as contemplated by the Enquiry Officer;

n) The inspecting officer had not raised the issue of dealing with the unregistered sub-broker. The Enquiry Officer has drawn an inference that Sureka Investments acted as a sub-broker. No evidence has been brought nor any circumstantial support has been advanced for drawing such inference. It is only in February 2002 that the said Sureka Investment in fact got registered as a sub-broker and started undertaking sub-broker activity;

o) the Company (the said broker) had been introducing its money from time to time in client account as a means of working capital and moreover the brokerages earned were also being accumulated in the clients account. Any outside cheques directly from clients account is due to extremely urgent situation out of own funds lying in the client account has not been with any ulterior motive. The broker has a cash credit limit with the said account. In any event, it has put in place checks and compliances to ensure that even inadvertent technical lapses do not occur. It has put in place robust back office system which will withstand the scrutiny of any future inspection or investigation by SEBI or NSE;

p) the enquiry officer has expressed dis-satisfaction in the margin collection mechanism in connection with Mr.Alok Khetan and Sureka Investments. It is submitted that as a risk containment measure, each client is assigned an exposure limit beyond which we have never permitted the client to trade. As a measure of maintaining of a good relationship with the client, the margin payments to the Stock Exchange were being funded by us from our own account. While this was a widespread industry practice, after the SEBI Circular dated February 4, 2000, we have revamped our margin collection system and now collected margin from every client. This is not subsisting breach at all.

4.0 Hearing

4.1 An opportunity of personal hearing was given to the said broker on 25.3.2003 when Mr.Bhavani Shankar Rath and Mr.Bijay Mumuria its Directors alongwith Shri Somsekhar Sundaresan, Advocate appeared before me. Mr.Sundaresan reiterated the submissions made in the reply dated 11.1.03. He further submitted that there is no statutory requirement of issuing contract notes to the clients. He requested that in view of the submissions, the major penalty in the matter may not be imposed.

5.0 Findings –

5.1 I have taken into account the facts and findings recorded in the enquiry officer's report, the oral and written submissions on behalf of the said broker and the relevant material available on record. My findings on the issues in the matter are as under -

5.2 Not maintaining the Order Book.

5.2.1 Vide SEBI Circular no.SMD/POLICY/IECG/1-97 dated 11.2.97 it has been specified that the brokers shall maintain record of time when the client has placed the order and reflect the same in the contract note alongwith the time of execution of the order. In terms of Regulation 6.1.1 of the NSE Capital Market Segment – Part A (hereinafter referred to as 'the NSE Regulations'), every trading member shall comply with all relevant Statutory Acts including the Securities Contracts (Regulation) Act, 1956, Securities Contracts (Regulation) Rules, 1957 and SEBI Act and rules, regulations and guidelines made thereunder and the requirements of directives and guidelines issued by the Central Government and any statutory body. In terms of regulation 6.1.3 (e) of the NSE Regulations (as applicable during the relevant time) every trading member shall maintain order book reflecting inter alia the following:

- i) Identity of the person receiving the order.
- ii) Date and time of the Order.
- iii) Name of the person placing the order.
- iv) Name of the client, description and value of securities to be bought and sold.

- v) Terms and conditions of the order stating particularly the price / rate limit or price / rate related instructions and time limit of the order etc.

As per Clause B (1) of the Code of Conduct as specified in Schedule II read with Regulation 7 of the said Regulations, it is the obligation of a stock broker that he faithfully executes the orders for buying and selling of securities for clients at the best available market price. The time when the order is placed and the time when the order is executed is very important. The trading system at the stock exchange can only show the time of execution of the order and not the time when the order was placed by the client. I find that before the enquiry officer the said broker has submitted that due to fear of volatility and price changes it is not possible to prepare separate records. I do not find any merit in these submissions of the said broker and also in the submissions made by its reply dated 11.01.2003 that it received orders on a real time basis and the order book could be created electronically by taking print out at the end of the day therefore it did not maintain the order book, since during the relevant period it was under the obligation to maintain the order book containing the particulars as mentioned above. Even when the broker received orders over phone it could maintain the said particulars in the order book. The order book is necessary for establishing as to when the order was placed and also the facts as mentioned above namely the name of the client, description and value of securities, terms and conditions of the order etc. These particulars are important to ascertain as to whether the stock broker has acted faithfully with the client, had acted with due skill and care etc. The requirement has been made optional later on. I find that the said broker has not maintained the order book and has violated the above mentioned SEBI circular no.SMD/POLICY/IECG/1-97 dated 11.2.97 and regulation 6.1.3 (e) of the NSE Regulations. In this regard the said broker has violated 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.

5.3 Non maintenance of Sauda Book

I agree with the findings of the Enquiry Officer that even though the trades of Alok Khetan operating from a terminal are duly reflected on a said broker's counter and confirmed on daily basis, nevertheless, it does not obviate the need to maintain the sauda book which is a statutory requirement. In terms of rule 15(1)(a) of the SC(R)R read with regulation 17(1)(a) it is statutory obligation of a stock broker to maintain the register of transactions i.e. the sauda book. However, in view of the findings given by the enquiry officer that taking into account the total volume of transactions which is Rs.10 lakhs annually as against the total turnover of 1,95,800 lakhs i.e. .05% of the turnover, the matter is not viewed seriously though the said broker is directed to comply with statutory requirements.

5.4 Non issuance of contract notes to Alok Khetan and Sureka

Investments.

5.4.1 Clause B(2) of the Code of Conduct as specified in Schedule II read with Regulation 7 of the said Regulations provides that a stock broker shall issue without delay to his client a contract note for all transactions in the form specified by the stock exchange. By SEBI circular no. SMD/(B)/104/22775/93 dated 29/10/1993 it was advised that SEBI will take a serious view if the deficiencies inter alia with respect to non issuance of contract notes to clients etc. are observed during the SEBI inspections. By the circular no.SMD/SED/CIR/93/23321 dated 18/11/1993, the SEBI has specified the norms regarding Regulation of Transactions Between Clients and Brokers and it has been made compulsory for all the brokers to issue contract notes for purchase / sale of securities to their clients within 24 hours of the execution of the contract. By the said circular the exchanges had been advised to make necessary provisions in their bye-laws and regulations for the purpose of regulation of transactions between clients and brokers as per the norms specified in the said circular. Regulation 3.5 of the said NSE Regulations provides that the members shall issue the contract notes for purchase / sale of securities to a constituent as specified in Annexure II and shall issue in the manner and within such time as prescribed by the exchange. Rule 15 (2) (b) of the SC(R)R and regulation 17 (1) (i) of the said regulations require every stock broker to keep and maintain the counter foils or duplicates of the contract notes issued to clients. Regulation 6.1.16 of the said NSE Regulations also requires every trading member to keep copies / duplicate of the contract notes issued by the member and details of statements which are required to appear on contract notes. These provisions clearly suggest that a stock broker has to compulsorily issue the contract notes to clients and keep and maintain the counter foils or duplicates thereof. Therefore, the submission that there is no provision requiring issuance of contract note is rejected. Vide SEBI circular No. SMD/POLICY /IECG/1-97 dated 11.02.97 requires every stock broker to maintain record of time when the client has placed the order and reflects the same in the contract note along with the time of execution of the order. It was directed that the stock exchange will initiate immediate action on the same. This requirement has to be fulfilled without any deviation. I find that this is a mandatory requirement and has to be complied with by every stock broker. In view of these findings, I find that the submission of the said broker that Mr. Alok Khetan was doing arbitrage business and was getting all details daily through net report, settlement bill, financial ledgers, daily position, etc. and he had requested not to issue contract notes is not maintainable and hence rejected. 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 skill, care and diligence in the conduct of all his business. I find that by not issuing contract notes to its clients as found during inspection and enquiry, the said broker has violated the above mentioned rules, regulations, SEBI circulars and NSE Regulations. In view of the above findings the other submissions that the error is technical etc. are also not maintainable.

5.5 Non maintenance of margin deposit book

5.5.1 The enquiry officer has noted that the said broker had replied that the margin payable was downloaded from the exchange system and maintained. In its reply dated 11.01.03 the said broker has submitted that none of the clients were paying margin money though a blank Margin Deposit Book was kept. I find that the Exhibit 7 of its reply is a page of paper titled "MARGIN DEPOSIT BOOK". This purported Margin Deposit Book is not authenticated. Moreover, it does not appear to contain any column regarding statements of margins. It can not suggest with reasonable certainty that the Margin Deposit Book was maintained by the said broker. Further, the submission that now the said broker is collecting margin and maintaining the Margin Deposit Book suggest that the said broker was not maintaining the said document during the relevant time.

5.5.2 As per SEBI circular SMD/SED/CIR/93/23321 dated November 18, 1993, it is provided that the brokers shall buy / sell securities on behalf of clients only on receipt of margin of minimum 20% on the price of the securities proposed to be purchased unless the client already has an equivalent credit with the broker. In terms of Regulation 17(1)(k) of the said Regulations a stock broker is required to maintain the Margin Deposit Book. It is the statutory requirement prescribed under the said Regulations and

every stock broker is under obligation to comply with it. 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. The submission of the said broker that it had had not collected margin and the margin payable is downloaded from the exchange system is not acceptable. I find that the said broker has violated the provisions of Regulation 17 (1) (k) of the said Regulations which prescribes the obligation of a stock broker to maintain the Margin Deposit Book.

5.6 Non maintenance of Document Register

5.6.1 In terms of rule 15(1) (g) of the SC(R)R read with regulation 17 (1) (g) of the said Regulations, every stock broker is required to maintain the document register including particulars of shares and securities received and delivered. I find that these provisions require inclusion of particulars of shares/securities. Such particulars of shares/securities definitely include distinctive number of the securities. In view of these statutory provisions, I find that the submission of the said broker that there is no provision of law requiring distinctive number to be maintained in a document register is not maintainable and hence rejected. I agree with the findings of the Enquiry Officer and hold that the said broker has violated these provisions.

5.7 Client agreement form not properly filled up

As per statutory requirements as stipulated in SEBI Circular no. SMD/POLICY/IECG/1-97 dated February 11, 1997; the stock brokers are required to maintain a database of their clients. It has been further prescribed vide circular no SMD/POLICY/CIR/5-97 dated April 11, 1997 that it would be the responsibility of the broker to provide for clients details as and when need arises. For this purpose an uniform format of client Registration Form and Broker- Client Agreement has been developed by SEBI and provided to all the stock exchanges with advise to implement the said requirement with immediate effect and complete the client registration before May 31, 1997. I agree with the findings of the enquiry officer that Client identification is important since that makes it easier for the audit trail to identify the clients behind the transactions. Details like bank account, PAN number, introducer photograph, proof of residence etc would establish the credentials of the clients and would be relevant to determine whether the said broker had acted in good faith and without negligence before doing business for a client. I find that the said broker has not taken the client registration forms duly filled in and hence violated the SEBI circulars SMD/POLICY/CIR/1-97 dated February 11, 1997 and SMD/POLICY/CIR/5-97 dated April 11, 1997.

5.8 Dealing with unregistered sub-brokers.

5.8.1 In its reply dated 11.01.03, the said broker has submitted that the charge relating to dealing with un-registered sub-brokers is contrary to facts. It is further submitted that the inspecting officer has not raised this issue at the time of inspection but has alleged in his letter for communication of findings. The enquiry officer has drawn an inference that it is probable that the Sureka Investments acted as a sub-broker and in all probability dealt with ultimate clients. Neither has evidence of any nature being brought to bear nor has any circumstantial support been advanced for drawing such an inference. In this regard, I find that vide inspection report para 5.3 the inspection team has found that the said broker's second largest client M/s. Sureka Investment who is based in Bhubaneswar, has been provided with a trading terminal by the said broker. The total turnover of this client is approximately Rs. 72.96 crores in the year 1999-2000. From the volume of transactions it appears that said Sureka Investment may be a sub-broker of the said broker. Therefore, I reject the contention that the charge is contrary to facts.

5.8.2 The enquiry officer has found that in view of the size of the volumes traded and admission of the said broker that he has traded with Calcutta Stock Exchange brokers indicate that the said alleged client was not merely ordinary clients but unregistered sub-brokers. Vide its reply dated 11.01.03, the said broker has submitted that it is only in February 2002 that the said Sureka Investment in fact got registered as a sub-broker and started undertaking sub-broker activity. This submission itself corroborates that the said Sureka Investment was an unregistered sub-broker during relevant time. 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. Further, vide circular No. SMD/ POLICY /CIR-/03/98 dated January 16, 1998 the stock brokers were advised to obtain certificate of registration to act as a sub-broker through the members of other exchanges. I find that the said broker has violated the mandatory requirements of SEBI circulars as recorded by the enquiry officer. The said broker is also under obligation to obtain client registration form from the clients containing the details of the clients. It is the obligation of the stock brokers to ensure that they do not deal with unregistered sub-brokers.

5.9 Non segregation of client's money and own funds.

5.9.1 By the circular no. SMD/SED/CIR/93/23321 dated November 18, 1993, the SEBI has specified the norms regarding 'Regulation of Transactions Between Clients and Brokers' and 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. Regulation 4.4.12 of the NSE Regulations provides that in addition to guidelines issued by SEBI relating to the Regulation of Transactions between Clients and Brokers, the member shall at all times keep the monies of the constituent in a separate bank account. Regulation 6.1.4 (b) of the NSE Regulations provides that it shall be compulsory for all trading members to keep the money of the clients in a separate account and their own money in a separate account. No payment for transactions in which the trading members is taking position as a principal will be allowed to be made from the clients account by the above mentioned circular and regulation 6.1.4 (c) it has been further provided that no money shall be drawn from clients account other than money properly required for payment to or on behalf of the client for or towards payment of a debt due to the member from the clients or money drawn on client's authority or money in respect of which there is a liability of clients to the trading member. 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.

5.9.2 I find that except in respect of two instances relating to bank guarantee commission as found by the Enquiry Officer, in respect of other 8 instances, as cited in the Enquiry Report, the submission of the said broker is not satisfactory. It is observed that the said broker has made payments from clients account towards payment for computers, cash withdrawals,

gratuity fund, loan etc. This is clearly in violation of the above mentioned SEBI circular and the NSE Regulations. As per these provisions money from the clients' account can be drawn only for the purposes as specified in the said circulars and NSE Regulations. Any other emergent situation is not acceptable for withdrawing money from the clients account for the purposes of computer etc. Therefore, I find that the said broker has committed the violation as observed in the enquiry report and has used the clients money towards the expenses like computers, cash withdrawals, loan refund, fees, gratuity fund, loan etc which is in violation of the SEBI circular and the NSE Regulations.

5.10 Non collection of margins

I find that the said broker Margins are imposed by the exchange/ SEBI as an important tool for risk containment measures. Collection of margins as prescribed by SEBI guidelines is a risk containment measure which should be strictly adhered to. As per SEBI Circular no.SMDRP/Policy/Cir-35/98 dated 4.12.98 it is mandatory for the stock brokers to collect margins from clients in all cases where the margin in respect of the client in the settlement, would work out to be more than Rs.50,000/-. The margin so collected is required to be kept separately in the client bank account and utilized for making payment to the clearing house for margin and settlement with respect to that client. Vide circular no.SMDRP/POLICY/CIR-7/2000 dated 4.2.2000, the requirement of collecting margins in respect of the client in a settlement, was increased from Rs 50,000/- to Rs.1,00,000/-. Thus, in all cases where the margin in respect of a client in a settlement would work out to be more than Rs.1,00,000/-, the member brokers shall have to mandatorily collect the margins from the client. I agree with the findings of the Enquiry Officer and hold that the said broker has violated this requirement of collecting margin from the clients.

6.0 In terms of rule 4 of the Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Rules, 1992, the Board may grant a certificate to a stock-broker subject to the following conditions inter alia that he shall abide by the rules, regulations and bye-laws of the stock exchange or stock exchanges of which he is a member. As found hereinabove the said broker has violated the NSE Regulations. Therefore, I find that the said broker has also violated the condition of the certificate of registration as provided in rule 4(b) of the SEBI (Stock Brokers and Sub-Brokers) Rules, 1992.

6.1 In view of the above findings, I hold that the said broker has violated –

- (a) Rule (15) (1) (g) of the SC (R) R,
- (b) Rules 4 (b) of the SEBI (Stock Brokers and Sub-Brokers) Rules, 1992,
- (c) Regulation 17 (1) (g) and (k) of the said Regulations and clauses A(5) and B(2) the Code of Conduct as specified in Schedule II read with regulation 7 of the said Regulations,
- (d) SEBI directives as contained in the circulars as found hereinabove,
- (e) The NSE Regulations as found hereinabove.

7.0 Whether the violations are technical –

7.1 The said broker has submitted, in respect of all the violations, that they are technical and minor and has not adversely affected the interests of the investors nor has it obstructed the promotion of the development of the securities market. In this regard, I find that as 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 (the rules), every stock broker is under obligation to comply with the statutory requirement prescribed under the Rules, Regulations and Bye-laws of the stock exchange (s) of which he is a member.

7.2 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 without attracting any action, the measures taken by SEBI for regulation of the stock brokers would be rendered nugatory and the regulatory function would be jeopardized. The requirements regarding margin collection, segregation of client's money and own funds or dealing with unregistered sub-brokers are provided as measures of risk containment and to provide transparency and fairness in the transactions. The requirements regarding maintenance of records etc. have been mandatorily provided to ensure that the business and conduct of the intermediaries are undertaken on the basis of sound business principles and to ensure that the regulator can regulate the business of stock brokers through inspections / enquiries.

7.3 It is to be noted that the violations by a stock broker which is regulated /

prohibited for the purpose of regulation of its business, 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 said brokers of the stock Exchange shall adhere to the bye-laws of the Exchange.

7.4 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. Regulation 4.5.1 of the NSE Regulations provides that the trading said broker shall at all times subscribe to the code of conduct as prescribed by the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992.

8.0 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(2), of the Code of Conduct as specified in Schedule II read with Regulation 7 of the Regulations and Rules 4(b) of the SEBI (Stock Brokers and Sub-brokers) Rules, 1992, Rule 15 (1) (g) of the SC(R)R and Regulation 17 (1) (g) and (k) of the said Regulations, SEBI directives contained in the circulars and the NSE Regulations 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.

8.1 I find that the said broker has committed several violations as observed above and has not taken due care and diligence in observance and compliance of the statutory requirements 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 Proceedings Regulations. Looking into the violations committed by the said broker, I am satisfied that to secure the proper management of the stock broker and also in the interest of the securities market a penalty of suspension of certificate of registration for a period of four months be imposed as recommended by the enquiry officer. 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 registration no. INB 231075830 of M/s Sumedha Fiscal Services Ltd., a member of the National Stock Exchange Limited, be suspended for a period of four months.

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

DATE : 19.5.2003

PLACE: MUMBAI

G. N. BAJPAI

CHAIRMAN

SECURITIES AND EXCHANGE BOARD OF INDIA