

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

UNDER REGULATION 13(4) OF SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002, AGAINST M/S.PRAKASH K. SHAH SHARES & SECURITIES PVT. LTD.

1.0 BACKGROUND OF THE CASE :

- 1.1 M/s.Prakash K. Shah Shares & Securities Pvt. Ltd. (hereinafter referred to as the broker) is a member of Bombay Stock Exchange (hereinafter referred to as BSE) and registered with Securities and Exchange Board of India (hereinafter referred to as SEBI) vide registration no. INB010997333.
- 1.2 An inspection of books of accounts, documents and other records of the broker was conducted in the second week of November, 2000. A copy of the inspection report was forwarded to the broker by SEBI vide letter dated 9.3.2001. The broker submitted its reply vide letter dated 17.5.2001 and on not being satisfied with the reply of the broker vis-a-vis the inspection report, an enquiry officer was appointed vide Order dated 14.3.2002 to conduct an enquiry into the contravention/s alleged to have been committed by the broker.

2.0 ENQUIRY REPORT AND RECOMMENDATION :

- 2.1 The enquiry officer, after conducting the enquiry as per the procedure prescribed submitted a report dated 31.1.2003. The enquiry officer concluded that the broker had committed irregularities pertaining failure to obtain consent from the clients for principal to principal transactions, failure to issue contract notes for Vyaj Badla transactions and for transactions done by jobber with whom the broking entity shares profit and losses, dealing with un-registered sub-brokers, failure to report cross deal transactions to the stock exchanges, failure to issue contract contract notes in Form 'B' for the transactions done on principal to principal basis, contract notes do not bear pre printed serial numbers and failure to ensure full particulars on the acknowledgements of the duplicates of the issued contract notes and client agreement related irregularities. The enquiry officer recommended that the registration of the broker be suspended for a period of four months.

3.0 SHOW-CAUSE NOTICE AND HEARING :

- 3.1 Pursuant to the above, a show cause notice dated 11.02.2003 was issued to the broker along with a copy of the enquiry report. The broker submitted a reply vide letter dated 15.3.2003 and also sought an opportunity of personal hearing which was granted to the broker on 31.05.2003. The representatives of the broker appeared before me and submitted a letter dated nil which contains the submissions of the broker.

4.0 CONSIDERATION OF THE ISSUES :

- 4.1 I have taken into consideration the enquiry report and the submissions made by the said broker vide letters dated 15.03.2003 and a letter dated nil which was submitted during the course of personal hearing held on 31.05.2003. I proceed to examine the same and my findings thereon are as mentioned below.

5.0 ALLEGATION AND REPLY :

- 5.1 As regards the failure to obtain consent from the clients for principal to principal transactions, the broker vide letter dated nil submitted that only 5 transactions were "principal to principal transactions" out of 32 transactions pointed out by the enquiry officer. The broker also stated that the confirmation letters from clients for the 27 transactions were submitted to SEBI vide letter dated 15.03.2003. Further, the broker also enclosed an extract of the Sauda Book in support of his submission.

5.2 FINDING :

I find that the broker has admitted the failure to obtain consent from the clients for principal to principal transactions in respect of 5 transactions as pointed out by the enquiry officer which is in violation of clause (c) of sub-rule (2) of rule 15 of Securities Contracts (Regulation) Rules, 1957. An examination of the extract of the Sauda Book and reply of the broker indicates that, although, the remaining 27 transactions may not be on principal to principal basis, these have been executed by the broker between its two clients which are cross deals and therefore, the conduct of the broker is in violation of clause (c) of sub-rule (2) of rule 15 of Securities Contracts (Regulation) Rules, 1957 read with the circular No. SMDRP/POLICY/CIR-32/99 dated September 14, 1999 issued by SEBI.

6.0 ALLEGATION AND REPLY :

As regards failure to issue contract notes for Vyaj Badla transactions, the broker vide the said letter submitted that Vyaj Badla transactions are distinct from normal Sale & Purchase transactions and these types of transactions are now not permitted. The broker further submitted that the Vyaj Badla transactions are entered at the end of the settlement and

same transaction is reversed inclusive of Badla Charges at the start of the next settlement at a special making up price fixed by the Stock Exchange, Mumbai and the special making up price of scrip for every settlement is determined by the Stock Exchange, Mumbai and officially published in the Bulletin of the Stock Exchange and these transactions are given effect invariably at that special making up price only. The broker also submitted that, after Vyaj Badla transactions, the settlement process is completed and the bills are prepared and are handed over to the clients on the next working day so that they know the net amount receivable / payable of the previous settlement.

6.1 **FINDING :**

The reply of the broker is not convincing inasmuch as in terms of clause B (2) of the Schedule II of SEBI (Stock Brokers and Sub Brokers) Regulations, 1992 (hereinafter referred to as "the said regulations"), a stock broker is required to issue contract notes for all transactions done by him. I find that there is no exception provided to this provision of law. Therefore, failure to issue contract notes in respect of Vyaj Badla transactions constitutes violation of law. Thus, I hold the broker guilty of violation of clause B(2) of the Code of Conduct as contained in Schedule II read with regulation 7 of the said Regulations and also SEBI's circular SMD/SED/CIR/93/23321 dated 18.11.1993. I hold the broker guilty of violating byelaw 247A(4) of the Byelaws of BSE also.

7.0 **ALLEGATION AND REPLY :**

As regards the failure to issue contract notes for transactions done by jobber with whom the broking entity shares profit and losses, the broker vide the said letter, inter alia, submitted that they are using BSE approved 'comtek' brand software for their back office work. This software does not have any contract note format to be used for the businesses done with jobbers. It only provides " Form 55" for calculating profit / loss on transactions carried out with jobbers. Further, to the best of their knowledge and information, there was no market practice to issue contracts for transactions done with jobbers. The broker further submitted that jobbers are market makers and not the investors and they themselves execute trade on the BOLT terminal. It was further submitted that the status of a jobber is different from a client and the individual client registration form filled in by them specifically mentions their occupation as jobber. The broker also submitted that jobber normally clicks the transactions where he finds spread between a sell and purchase price and reverses his position immediately and the transactions are numerous in a day. It was also submitted that to facilitate their trade, they had allotted them an exclusive terminal to execute trade by themselves and they do not charge any brokerage and share profit and loss arising out of their trade.

7.1 **FINDING :**

It is observed that the broker has admitted that the jobbers too fill in the individual client registration form mentioning their occupation as jobber. It is also noted that the broker had allotted the jobbers an exclusive terminal to execute trade themselves in order to facilitate the trading of the jobbers. It indicates that the trades of the jobber were on their own account, not on the account of the broker and these so called jobbers are none other than clients trading in the name of jobbers in own account. The conduct of the broker in its failure to issue the contract notes to all clients is in violation of clause B (2) of the Code of Conduct as specified in Schedule II read with regulation 7 of the said Regulations and also SEBI's circular SMD/SED/CIR/93/23321 dated 18.11.1993.

8.2 **ALLEGATION AND REPLY :**

As regards, the charge of dealing with un-registered sub-brokers, in the case of two clients viz. Shri Deepak Shah and M/s Binti Finance the securities were not received directly from them but from their clients. Securities were being received and transferred directly to clients of the above two entities though the contract note was issued in favour of the above entities. The following are the details of the transfers of shares:

Shri Deepak Shah (10001904)

S. No.	Sett No.	Scrip	Pay-in recd from (Client ID)	Qty
1.	19	India Cement	10064151	2000
2.	19	Novaritis	10064151	100
3.	32	HPCL	11262547	100
4.	32	Videocon Int.	10040786	8
5.	33	Wool Worth Ltd.	10042912	400
6.	33	Bhandari Udyog	10001689	200
7.	33	Gold Store Tech	10599475	50
8.	34	DSQ Soft.	10599475	50

S. No.	Sett No.	Scrip	Pay-in recd from (Client ID)	Qty
9.	34	DSQ Soft.	10064151	50
10.	34	Gold Store Tech	10599475	50
11.	34	SAIL	10064151	3900
12.	34	Wool Worth Ltd.	10042912	985

M/s Binti Finance (10044711).

S. No.	Sett No.	Scrip	Pay-in recd from (Client ID)	Qty
1.	20	Reliance Petro	10285102	200
2.	32	Nexus Software	13000034	200
3.	34	Amara Raja Batt.	12812398	2500
4.	34	Reliance Petro	10165824	100

The broker vide the said reply, inter alia, submitted that their main activity of stock broking is retail business due to which there are numerous trades and huge clientele business and therefore they are under tremendous pressure to adhere to the fixed time schedule of the stock market operations. It was also submitted that in case of sale of shares by the clients, the client directly credits shares to their pool account without any necessity of their prior consent or approval as the normal procedure and the broker receives the demat statements only after the end of the settlement i.e. after pay – in and pay –out is over. The broker further submitted that they had no knowledge of non receipt of shares from their clients demat account.

8.3 FINDING :

The above tables explicitly prove that the Shri Deepak Shah and M/s Binti Finance are dealing on behalf of their clients. Thus, the broking entity is dealing with un-registered sub-brokers inasmuch as M/s. Binti Finance and Mr. Deepak Shah had acted as sub brokers in the aforesaid transactions without obtaining registration from SEBI.

Also a perusal of the agreement of broking entity with M/s Binti Finance, a reference was attached with it from M/s Kamlesh J. Shroff, member of BSE which showed that M/s Binti Finance is a sub-broker registered with them. From the analysis of the Demat statements and the Pay-in and Pay-out statement (as mentioned above), it was found that M/s. Binti Finance and Shri Deepak Shah were doing business for their clients and thus dealing as un-registered sub-brokers.

Therefore, I find that the broker has violated the provisions of Section 12 of SEBI Act, 1992 read with SEBI's Circulars SMD-1/3118 dated 27/12/93, SMD/OPG/AA/ 1020/96 dated 14/03/96 and SMD/Policy/CIR/03/98 dated 16/01/98.

9.0 ALLEGATION AND REPLY :

9.1 As regards, the charge that the broker has executed cross deal in their office and failed to report these transactions to the exchange, the broker vide the said letter, inter alia, submitted that the value and quantity of the transactions do not qualify as negotiated or cross deal in terms of the circular dated 04.08.98 issued by SEBI.

9.2 FINDING :

The contention of the broker is not satisfactory inasmuch as the circular No. SMDRP/POLICY/CIR-32/99 dated September 14, 1999 stipulates that all negotiated deals including cross deals irrespective of quantity or value are not permitted and all such deals are required to 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. In view of this, I hold the broker guilty of violating the provisions of circular No. SMDRP/POLICY/CIR-32/99 dated September 14, 1999 issued by SEBI read with clause A (5) of the Code of Conduct as specified in Schedule II read with regulation 7 of the said Regulations.

10.0 ALLEGATION AND REPLY :

10.1 As regards, the allegation that Form B contract notes were not issued for transactions done on Principal-to-Principal basis, the broker submitted to the enquiry officer that "through the oversight that in respect of transaction done between principal to principal "A" Form contract issued by mistake, but there was no dispute regarding the transactions as principal to principal and the transactions was carried out and no claim or complaint or any nature whatsoever was made by us. The said principal to principal transactions were reported in the Stock Exchange, Mumbai. We may further inform you that we have already stopped transactions as principal to principal basis."

10.2 FINDING :

The conduct of the broker in not issuing contract notes in Form "B" for principal to principal transactions is violative of the circular No. SMD(B)/104/22775/93 dated 29.10.1993 read with clause A (5) of Code of Conduct as specified in Schedule II read with regulation 7 of the said Regulations.

11.0 ALLEGATION AND REPLY :

11.1 As regards the charge that the contract notes do not bear pre-printed serial numbers but generated on daily basis through computer software the broker submitted that "in all other stationary there were no pre-printed numbers. After your enquiry we have already given instructions to our software programmer to incorporate under the system to print the contract number serially in conformity with your direction. We may inform you that we have not issued any duplicate contract notes in respect of any transactions effected by us."

11.2 FINDING :

The system of continuous pre-printed serial numbers is to prevent the possible misuse of contract notes such as pre-dating of a contract. It is clear that the broker failed to maintain pre-printed serial numbers on the contract notes and I hold the broker guilty of violating the provisions of clause A (5) of Code of Conduct as contained in Schedule II of the said regulations read with the circular no.SMD/MDP/CIR/043/96 dated 5.8.96 issued by SEBI.

12.0 ALLEGATION AND REPLY :

12.1 As regards the charge that the acknowledgement of the clients on the duplicates of the contract notes issued, does not contain the date, the broker submitted that "according to the SEBI Guidelines we have delivered the contract to the client within 48 hours from the date of the contract and the same is acknowledged by the client. If no date is put along with the acknowledgement it is deemed under law that the client has received the contract on the date mentioned in the contract. However, we will be careful now to take the dates along with the acknowledgements."

12.2 FINDING :

In the absence of mentioning of date on contract note, it is difficult to ascertain whether the contract notes were issued within 24 hours from the execution of the transaction. Therefore, I hold that the broker has violated the provisions of clause B (2) of Code of Conduct as contained in Schedule II of the said regulations.

13.0 ALLEGATION AND REPLY :

The following allegations were made vis-à-vis the Client Agreement -

- a) The agreement in most of the cases is not executed on a stamp paper.
- b) The agreement does not bear the date on which the agreement was signed.
- c) Also, the agreement fails to mention the name of the client with whom the agreement is signed. However, the signature of the clients are present.

The broker submitted that "regarding irregularities in client's agreement we may inform you that we have completed all the agreements on stamp papers and the same have been duly executed by the client and ourselves. You can verify the same at any time without notice."

13.1 FINDING :

The reply of the broker is vague and did not answer about the agreements executed in the past with the above irregularities. Thus I find that the broker has violated SEBI's Circular SMD/Policy IECG/1-97 dated 11/02/97 & SMD/POLICY/CIRCULAR/5-97 dated 11.04/97 read with clause A (5) of Code of Conduct as contained in Schedule II of the said regulations.

14.0 CONCLUSIONS :

14.1 In view of the above, I do not see any reason to differ with the findings of the enquiry officer. I am fully convinced that the broker has committed irregularities as found above.

14.2 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. In terms of rule 4(b) of the SEBI (Stock Brokers and Sub-brokers) Rules, 1992 one of the conditions for grant of certificate of registration is that the broker shall abide by the rules, regulations and bye-

laws of the stock exchange or stock exchanges of which he is a member. In view of the findings as mentioned in paras 4.0 to 13.1, I conclude that the said broker is guilty of having violated,

- (a) Section 12 of Securities and Exchange Board of India Act 1992,
- (b) Clause (c) of sub-rule (2) of rule 15 of Securities Contracts (Regulation) Rules, 1957.
- (c) The provisions of clauses A(5) and B(2) of the Code of Conduct as specified in Schedule II read with Regulation 7 of SEBI (Stock Brokers and Sub-brokers) Regulations, 1992,
- (d) The conditions of registration specified in Rule 4(b) of the SEBI (Stock Brokers and Sub-brokers) Rules, 1992,
- (e) SEBI's directives contained in the circulars as mentioned hereinabove.
- (f) Bye – Law No. 247A (4) of the Bye – Laws of BSE.

In view of the same, the said broker is liable for action under regulation 13(1)(b) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002.

14.3 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. It is to be noted that indulgence of the said broker in the transactions which are prohibited can not be allowed 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 every Stock Exchange shall adhere to the bye-laws of the Exchange.

15.0 ORDER :

15.1 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 requirement in conduct of its business as a stock broker. As regards the recommendation of the enquiry officer for taking a lenient view vis-a-vis the irregularities such as failure to issue contract notes in Form 'B' for the transactions done on principal to principal basis, contract notes do not bear pre printed serial numbers and failure to ensure full particulars on the acknowledgements of the duplicates of the issued contract notes and client agreement related irregularities. I feel that the said irregularities do not deserve any lenient view and the broker is liable for action even in respect of those irregularities. 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 four months as recommended by the enquiry officer 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 registration no. INB 010997333 of M/s. Prakash K. Shah Shares & Securities Pvt. Ltd. a member of The Stock Exchange, Mumbai be suspended for a period of four months.

This order shall come into force with effect from three weeks from the date of this order.

Place: Mumbai

Date : July 29, 2003

G. N. BAJPAI

CHAIRMAN

SECURITIES AND EXCHANGE BOARD OF INDIA