

SECURITIES AND EXCHANGE BOARD OF INDIA

CO/135/MIRSD/09/2003

ORDER UNDER REGULATION 13 (4) OF SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002 AGAINST M/s ENIGMA FINANCIAL SERVICES PVT. LTD. MEMBER, UTTAR PRADESH STOCK EXCHANGE.

1. M/s Enigma Financial Services Pvt. Ltd. is registered with SEBI as a stock broker (hereinafter referred to as 'the member') bearing SEBI registration no. INB 101023233 and is a member of Uttar Pradesh Stock Exchange (UPSE). An inspection of books of accounts, documents and other records of the member was conducted on 15.03.2001. During the inspection, several irregularities were found committed by the member.
2. The findings of the inspection were forwarded to the member vide letter dated 04.05.2001 advising the member to give his comments, if any. The member vide letter dated 30.06.01 replied to the said findings of the inspection report. On not being satisfied with the reply filed by the member an Enquiry officer was appointed vide order dated 19.07.2002 to enquire into allegations of violations against the member, inter alia, to the following:
 - (a) Violation of section 12 of Securities and Exchange Board of India Act, 1992 read with Rule 3 of SEBI (Stock Brokers and Sub-brokers) Rules, 1992.
 - (b) Violation of Rule 4 (b) & (d) of the SEBI (Stock Brokers and Sub-Brokers) Rules.
 - (c) Violation of Regulation 10(1) of SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992.
 - (d) Violation of Clause A(5) & B(1) of the Code of Conduct as specified in Schedule II read with Regulation 7 of the said Regulations;
 - (e) Violation of the Directives issued by SEBI vide circular nos. SMD/MDP/CIR/043/96 dated 05/08/96, SMD-1/23341 dated 18/01/93, SMD/POLICY/IECG/1-97 dated 11/2/97, SMD/POLICY/IECG/5-97 dated 11/04/97, SMD/POLICY/CIR-3/98 dated 16/01/98, SMD/RCG/CIR(BKG)/293/95 dated 14/03/95, SMDRP/POLICY/CIR/32-99 dated 14/09/99, SMD/POLICY/CIRCULAR/3-97 dated 31/3/97, SMD/SED/CIR/93/23321 dated 18/11/93, SMDRP/POLICY/CIR - 35/98 dated 04/12/98, SMDRP/POLICY/CIR-07/2000 dated 10/01/2000 and SMDRP/POLICY/CIR-11/99 dated 07/05/99;
 - (f) Notification no. SO/2561 June 27, 1969 issued by the Central Government under Sub Section (1) of Section 16 of Securities Contracts (Regulation) Act, 1956 read with the directives issued by SEBI vide its circular No. SMD/SED/93-30727 dated 13/12/93 and SMD/SED/3703/95 dated 16/10/95
 - (g) Rules, Regulations and Byelaws of UPSE as amended from time to time and directives of UPSE
3. The Enquiry Officer submitted his report on 28.01.2003. In his report, having regard to the gravity of the irregularities that have been established, the EO recommended suspension of certificate of registration of the member for a period of 4 months. The Enquiry Officer found that the member committed the following violations:
 - 3.1 The member has dealt with the member of other exchanges other than UPSE without seeking registration as a sub-broker.
 - 3.2 The member has dealt with un-registered sub-brokers.
 - 3.3 The member has done unauthorized carryforward transactions.
 - 3.4 Non-Maintenance of member client agreement
 - 3.5 Contract notes were not serial numbered; it doesn't have trade number and time of ordering and execution of trade.
 - 3.6 Conducted off the floor transactions

3.7 Duplicates of the Contract Notes were not acknowledged by the clients.

4. Consequent upon above, in terms of regulation 13(2) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as 'the said regulations') a show cause notice dated 24.03.2003 was issued to the member to show cause as to why the penalty as recommended by the enquiry officer should not be imposed on him. The member was advised to submit his reply, if any, within 15 days of the receipt of the show cause notice failing which it would be presumed that the member has no explanation to offer. The member was also asked to intimate along with the reply whether he desires a personal hearing. The member vide letter dated 07.05.2003 replied to the show cause notice dated 24.03.2003. The member made the following submissions:

- a) With reference to delay in payment of Turnover Fee to SEBI, the member stated that the enquiry officer considered their submission and in view of the delay which was not substantial recommended that the matter might be viewed leniently.
- b) Regarding dealing as unregistered sub-broker, the member submitted that this was done only as an experiment and the volumes traded were not substantial. The practice was discontinued within a short period of time.
- c) Regarding dealing with unregistered sub-broker, the member strongly denied that any of the names mentioned in communication of findings relied upon by the Enquiry Officer were sub-brokers and reconfirmed that all of them were portfolio clients. The member concluded that trading volumes and pattern of trading could not be taken as conclusive evidence.
- d) With respect to delay in transfer of shares, the member submitted that being in a small city they worked in an environment which was more friendly than formal and their clients insisted that they should hold payment/deliveries to be adjusted against subsequent sales/debits.
- e) With reference to unauthorized carry forward transaction the member submitted that their explanation in the matter was not considered in true light by the Enquiry Officer. The member further submitted that the difference in sale/purchase did not represent carry forward charges. Member contended that In the course of computerized trading countless trades match every minute and that the matching of quantity with the same member might be purely coincidental. It was argued that mostly the trades matched with the members who trade regularly and frequently and that the matching of such trades could only be natural.
- f) Regarding delayed payment to the clients, the member made similar submissions made in the matter of delayed deliveries to the clients. Further, the member submitted that they furnished to SEBI several letters from clients approving such trading practice.
- g) With reference to non-maintenance of client registration forms and broker client agreements, the member stated that they had already submitted before the Enquiry Officer that these defects had since been rectified.
- h) Regarding the irregularity that contract notes do not bear pre-printed serial numbers and no time regarding placement of orders and execution, the member stated that they had already clarified their difficulties before the Enquiry Officer.
- i) With respect to off the floor transactions, the member submitted that the lapse on their part was under the mistaken belief that the concerned BSE and NSE brokers reported the transactions and it was not incumbent on them to do the same and the transactions for full year 1999-2000 amounted to only 55 lakhs and no risk or default ever occurred because of this transactions.

- j) Regarding duplicate of contract note not acknowledged by clients, the member submitted that most of their clients were based outstation and that they either neglect or return acknowledged copies.

5. The member sought personal hearing while submitting as above. The member was given an opportunity of hearing on 6.6.2003. The member failed to avail the said opportunity. Further another opportunity of hearing was given on 19.6.2003. Shri Pankaj Arora, Director of member appeared and made submissions. During the course of the submissions, he made a request to grant him further time to file certain letters /documents. Accordingly, the member was granted 10 days time to grant the same.

6. The member vide letter dated 19.6.2003 while reiterating their earlier submissions made vide letter dated 07.05.2003 submitted certain documents.

7. I have carefully examined the facts and circumstances of the case. I have also carefully considered the Enquiry Report and the submissions made by the member vide letter dated 07.05.2003 and 19.6.2003. On appreciating the facts and circumstances of the case the findings are as under:

7.1 I find that the member dealt with DSM Stock brokers, member NSE and Meghna Securities, sub broker of NSE and BSE without being registered as sub-broker. The member admitted that he had dealt with the members of other stock exchanges in a small way on an experimental way and some transactions were executed for clients also as he could not disappoint the clients who wanted to trade on shares not listed at UPSE. I find that the volumes with DSM was Rs.54.69 lakhs. The argument of the member that it was an experiment and that he could not disappoint the clients who wanted to trade on shares not listed at UPSE is not justifiable by any standards. Therefore, I find that the member acted as an un-registered sub broker in violation of Section 12(1) of SEBI Act, 1992, Rule 3 of SEBI (Stock brokers and sub brokers) Rules, 1992 and SEBI Circular : SMD/POLICY/CIRS-11/97 dated 21.5.97 and Circular : SMD/POLICY/CIR-3/98 dated 16.1.98.

7.2 I find that the member had dealt with unregistered sub brokers. The member denied that the entities M/s. Pasha Stock Fintrade Pvt. Ltd., S.R. & Co. Pvt. Ltd., Ramsham & Co. and Vibhash Agarwal were unregistered sub brokers and stated that they were all portfolio clients. The member in their reply dated 7.4.2003 stated that Pasha Stock Fintrade Pvt. Ltd. was a manufacturer and whole sale dealer of sewing machines and if sought the member would approach the party to sign a letter or an affidavit that they never acted as a sub broker. However, I find that the submission of the member is not tenable in light of the fact that the trading volume and the pattern of the said entities is suggestive of their dealings as unregistered sub brokers. Further, the member vide letter dated 28.6.2003 furnished a document signed by Vibhash Agarwal stating that Shri Vibhash Agarwal did business with the member in his individual capacity as portfolio client and never acted as a sub broker on behalf on any other client. I perused the said document. The said document is produced as a matter of after thought. Therefore, I find that the member dealing with unregistered sub brokers is in contravention of SEBI Circular : SMD/POLICY/CIR-3/97 dated 31.3.97.

7.3 I find that the member indulged in unauthorized carry forward transactions. The list of 25 transactions entered into by the member is shown in the table below:

Sr. No.	Qty	Date	Rate	Scrip	Contra Broker	Qty.	Date	Rate
1.	150	14.8.2000	482.00	Satyam	PK Capital Securities	150	16.8.2000	482.00
2.	-150	14.8.2000	240.00	Tate	Kusum Stock Brokers	150	16.8.2000	240.00
3.	800	17.1.2000	129.10	RCFT	Atul Kanodia	-800	18.1.2000	130.10
4.	-400	17.1.2000	70.50	RELE	Ajay Securities	400	18.1.2000	71.10
5.	-500	17.1.2000	241.00	SBIN	Bansal Securities	500	18.1.2000	241.50
6.	-1000	15.1.2001	153.00	ACC	Jai Ram Dubey &	1000	16.1.2001	153.15
7.	600	26.12.2000	153.00	ACC	Saroj & Co.	-600	27.12.2000	153.00
8.	-200	8.1.2001	370.00	DSQS	Malay Inv & Fin	200	9.1.2001	370.75

9.	-500	26.12.2000	370.00	DSQS	Bharat K. & Co.	500	27.12.2000	370.75
10.	-200	8.1.2001	210.00	HIND	Akash Securities	200	9.1.2001	210.25
11	-1000	26.12.2000	203.00	HIND	Amit Jindal A	1000	27.12.2000	203.10
12.	250	2.1.2001	903.00	ITC	Kapoor & Co.	-250	3.1.2001	946.50
13	100	29.1.2001	410.00	DSQS	Anand Investors	-100	30.1.2001	431.25
14	1000	2.1.2001	42.50	Jain	Rakesh Chandra	-1000	3.1.2001	43.75
15	1500	8.1.2001	45.00	Jain	Prashant Jain	-1500	9.1.2001	42.00
16	1000	15.1.2001	42.00	Jain	BNK Investments	-1000	16.1.2001	42.10
17	-4000	2.1.2001	214.00	LT	Vinod Kumar & Co.	4000	3.1.2001	216.10
18	-2000	22.1.2001	263.00	Peso	Deep Kumar Agg	2000	23.1.2001	264.00
19	3000	29.1.2001	93.00	RCFT	Jai Ram Dubey & Co.	-3000	30.1.2001	93.00
20	-6000	2.1.2001	58.25	RELE	Vineet K. Tandon	6000	3.1.2001	58.45
21	-9000	15.1.2001	60.00	RELE	Vinod Kumar & Co.	9000	16.1.2001	60.80
22	-3600	26.12.2000	55.00	RELE	Vineet K. Tandon	3600	27.12.2001	53.15
23	-1000	29.1.2001	128.05	TIS	Jai Ram Dubey & Co.	1000	30.1.2001	128.35
24	-750	15.1.2001	133.00	TIS	ML Agarwal & Co.	750	16.1.2001	133.40
25	-1200	26.12.2000	259.00	ZEET	Bharat K. & Co.	1200	27.12.2000	259.60

The above table clearly shows that the transactions were closed on the last day of the settlement and was re-opened on the first day of the subsequent settlement. These transactions are in the nature of carry forward transactions and the members of UPSE are not authorized to conduct carry forward transactions. The members submission, vide letter dated 7.5.03, that in the course of computerized trading countless trades match everyday and that the matching of quantity with the same member might be purely coincident and that the trades matched with the members who trade regularly and frequently which could only be natural is not acceptable. I find that the matching of trades in so many instances with the same member and at the same price cannot be treated as natural. Therefore, the transactions entered into by the member are in violation of Notification No.SO 2561 dated 27.6.1969 issued by the Central Govt. under Section 16 (1) of Securities Contracts Regulation Act, 1956 read with the directors issued by SEBI Circular No.SMD/SED/93/30727 dated 13.12.93 and SMD/SED/3703 / 95 dated 16.10.95.

7.4 I find that the member delayed payments to clients. I find that the Enquiry Officer in his report dated 28.2.03 noted delayed payments to 13 clients in respect of various transactions. Further, the Enquiry Officer found that the member furnished authorization letters with respect to 5 clients only. The member during the course of personal hearing assured to submit authorization letters with respect to the remaining clients. The member vide letter dated 28.6.03 furnished 11 undated letters stating them to be authorization letters from the clients. On perusal of the said letters, it clearly appears that they are the products of after thought. As per SEBI Circular dated 18.11.1993, member broker shall make payment to their client or deliver the securities purchased within 2 working days of the pay out unless the client requested otherwise. Therefore, the said lapse of the member is in violation of the aforesaid circular.

7.5 I find that the member failed to maintain Client Registration Forms and Broker client agreements. I also find that during inspection the member admitted that the client registration form and the broker client agreement form in respect of several clients were not maintained. The member submitted before the enquiry office that these defects had since been admitted. I agree with the Enquiry Officer's findings that client identification is important since it makes easier for the audit trail to identify the clients behind the transactions. Details like bank accounts, PAN No., introducer etc. would establish the credentials of the clients and would be relevant to determine whether the member had acted in good faith and without negligence without doing business for a client. Therefore, I find that the omission of the member is in contravention of SEBI Circular SMD/Policy/CIR/5-97 dated 11.4.97.

- 7.6 I find that the contract notes issued by the member did not bear pre-printed serial nos. and time regarding placement of order and execution. The omissions of the member are in violation of SEBI Circular SMD/MDP/CIR/043/96 dated 5.8.96 and Circular SMD/Policy/IECG/1-97 dated 11.2.97.
- 7.7 I find that the member had conducted off the floor transactions with DSM Stock brokers, member NSE for Rs.54,69,241.90 paise for the year 1999-2000 and also with Meghna Securities for BSE and NSE. The member vide letter dated 7.5.03 submitted that the transactions for the full year 1999-2000 amounted to only 55 lakhs and that no risk or default ever occurred because of these transactions. I also observed that the member had entered into a cross deal while transacting for its client Karuna Arora and Banwarilal HUF.
- 7.7.1 I find that the member admitted the above instances. SEBI vide Circular dated 14.09.1999 banned all negotiated deals, cross deals etc. which include Off-the-floor transactions also. In the said circular it had been notified that all negotiated deals shall be permitted only if the said deals are executed on the screens of the Exchange i.e. the price and order match mechanism of the Exchange like any other normal trade.
- 7.7.2 The said decision was taken as negotiated deals are devoid of transparency requirements. They also do not contribute to price discovery at the stock exchange depriving the investors of the benefit of best price. Therefore, such deals militate against basic principals of stock exchange mechanism which is meant to bring large number of buyers and sellers together in a transparent manner. It is apparent from the above that the off the floor transactions were not put in the system of the Exchange by the member. This is in violation of SEBI Circular dated 14.09.1999. This kind of off the floor transactions tamper with price discovery mechanism of the exchange and such trading leads to interference with the fair and smooth functioning of the market. Such deals are also in violation of item 5 of clause A of Code of Conduct read with regulation 7 of Broker Regulations.
- 7.8 I find that the member did not maintain duplicates of contract notes duly acknowledged by clients. The member vide letter dated May 7, 2003 submitted that most of the clients were outstation based and either neglect to return acknowledged copies or some copies are lost in transit or misplaced. The submission of the member cannot be accepted as in terms of Rule 15(2) (b) of SCR Rules, 1957, every broker has to maintain duplicate copies of the contract notes issued to clients for a period of 2 years. By not maintaining duplicate copies of the contract notes with acknowledgement of investors thereon, the member violated Circular SMD/1/23341 dated 18.11.93 which stipulates that the broker should insist on the investors returning the duplicate copies of the contract notes duly signed by them.
8. I have no hesitation to agree with the findings of the Enquiry Officer. The above findings against the member, which include carry forward transactions and off the floor transaction cannot be taken lightly particularly when the same are in the nature of disturbing the equilibrium of the market and hindering the interest of investors and the development of capital market. In light of the findings I am not agreeable with the member's submission that there was no such intention to deliberately violate/contravene any rules and regulations of SEBI. The violations committed by the member are of serious nature hence the intention of the member becomes irrelevant.
9. I am satisfied that this is a fit case to impose major penalty suspending the registration of the member. Therefore, in exercise of the powers conferred upon me by Sub Section (3) of Section 4 of SEBI Act, 1992 read with sub-regulation (4) of Regulation 13 of the said Regulations, I hereby suspend the certificate of registration of M/s Enigma Financial Services Pvt. Ltd., for a period of four months. This order shall come into force after 3 weeks from the date of the order.

Place: Mumbai

Date: 26.09.03

G N BAJPAI

CHAIRMAN

SECURITIES AND EXCHANGE BOARD OF INDIA