

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

ORDER UNDER REGULATION 13 (1) OF SECURITIES AND EXCHANGE BOARD OF INDIA (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002, IN THE MATTER OF M/S.BAKLIWAL INVESTMENT, MEMBER NATIONAL STOCK EXCHANGE

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1.0 Background:

1.1 Bakliwal Investment (hereinafter referred to as 'the broker') a member of National Stock Exchange (hereinafter referred to as 'NSE') is registered with the Securities and Exchange Board of India (hereinafter referred to as 'SEBI') under certificate of registration no. INB 230922920.

1.2 SEBI conducted an inspection of the Broker through M/s. Kalyaniwala & Mistry, Chartered Accountants, who submitted their report on 7.5.2001 for the period 01.04.1999 to 30.09.2000.

2.0 Enquiry Proceedings:

2.1 After consideration of the inspection report, Chairman, SEBI vide order dated 31st January 2003 appointed an enquiry officer under Regulation 5 (1) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as "the said Regulations") to enquire into possible violations, inter alia, of SEBI (Stock Brokers and Sub Brokers) Regulations, 1992.

2.2 Enquiry Officer issued a show cause notice to the broker on May 21, 2003 in accordance with Regulation 6 of the said Regulations, alleging as follows:

2.2.1 Entries for the broker's own trading constituting 95% of the volume of trades were passed only after the inspection commenced.

2.2.2 Provision for tax for the interim period from April 1 to September 30, 2000 was not made by the broker.

2.2.3 Confirmations have not been obtained from banks, creditors, and debtors by the broker.

2.2.4 The broker had not 'time stamped' the order slips/records. The order time is not reflected in the contract notes. The only time reflected in the contract note is the time of keying in the order into the NEAT system.

2.2.5 Contract notes issued by the broker were not serially numbered, except for computer generated numbers on day to day basis, which have no control.

2.2.6 The contract notes were not issued within the specified time by the broker.

2.2.7 Consolidated Stamp duty was not paid for Settlement Nos. 30 and 34 of 1999 by the broker.

2.2.8 Brokerage account includes a credit of Rs. 14, 54, 592/- being amount received from Soba Infosec Private Limited as incentive against investment in Zurich Top 200 Fund.

2.2.9 With regard to 'know your client' requirement it was observed that Client registration forms were not completed or supporting documents were not in place for direct clients.

2.2.10 Order book was not maintained by the broker as required under SMD/Policy/IECG/1-97 dated February 11, 1997.

2.2.11 Broker failed to obtain agreements from all the constituents.

2.2.12 There were instances of delay in payment of funds. In the settlements selected, 26 instances of delays ranging from 10 to 322 days in payment of funds to the constituents were noticed.

2.2.13 There were instances of delay in delivery of securities. In the settlements selected, 3 instances of delays ranging from 6 to 49 days in delivery of securities to the constituents were noticed.

2.2.14 There were instances of one client's account being adjusted against another client for which no instructions / authorization was made available.

2.2.15 With regard to transactions with associate firms / companies separate set of ledger accounts as clients and others, was not maintained by the broker.

2.2.16 The broker failed to maintain a complaints register.

2.2.17 During the period April 1999 to December 2000 it was observed that clients bank accounts (A/c No. with Global Trust Bank, Mumbai and Janata Sahakari Bank Ltd., Pune) were used for purposes other than those specified under SMD/SED/CIR/93/23321 dated 18.11.1993.

2.2.18 The broker's gross exposure with reference to the networth computed as at March 31, 2000 was in excess of 12.5 times the base + additional capital as stipulated in SMD/SED/CIR/93/22570 dated October 21, 1993.

2.2.19 The networth as at September 30, 2000 was Rs.95 lacs.

2.2.20 From a review of the Ledger Accounts 10 instances of deals done outside the NEAT system were observed. Of these, 8 transactions were done by the broker on the Bombay Stock Exchange through another registered broker.

2.2.21 The broker failed to collect margins from his clients. The broker has also failed to comply with the requirements of issuing contract note in Form B, or reporting the trade and settlement thereof to the exchange.

2.2.22 There has been a delay by the broker in submission of the audited Balance Sheet and Profit & Loss Account for the year ended March 31, 2000 to the stock exchange.

2.3 The enquiry officer after considering the submissions of the broker submitted his report dated January 13, 2004 recommending a minor penalty of warning to the broker.

3.0 Show cause notice and hearing:

3.1 Subsequent to submission of the enquiry report, show cause notice dated January 29, 2004 was issued to the broker along with a copy of the enquiry report. The broker replied vide letter dated February 12, 2004 seeking an opportunity of personal hearing. However, since the broker did not reply to the charges contained in the Enquiry Report, the broker was advised to submit his detailed reply to the show cause notice. The broker vide his letter dated March 01, 2004 submitted its reply to the show cause notice. However, the broker has not sought any personal hearing.

4.0 Consideration of Issues:

4.1 I have considered the facts of the case, the findings of the Enquiry Officer, the reply of the broker to the show cause notice and other material on record. I find that:-

4.1.1 The Broker has not issued pre-printed contract notes as per SEBI guidelines. The Broker has submitted that his business mainly consists of arbitrage transactions and other clientele constituted of only 5%. The idea of issuing pre-printed contract notes is to avoid any misuse of contract notes. However, in this case, the broker had pre-dominantly dealt with arbitrage transactions and had only 5% of other clients.

4.1.2 Broker failed to pay consolidated stamp duty on time. Broker admitted that there has been a delay in paying stamp duty but submitted that it was only an oversight. I note that broker had paid consolidated stamp duty but with extra-ordinary delay.

4.1.3 Broker had a credit of Rs. 14, 54, 592/- in brokerage account received from Soba Infosec Pvt. Ltd. as incentive against investments in Zurich Top 200 Fund. It is noted that Soba Infosec Pvt. Ltd. has confirmed making the above payment towards incentive against investment in Zurich Top 200 Fund. However, this is the only instance of broker not keeping separate account.

4.1.4 The broker mis-used client account by adjusting one account with another without proper authorization. The broker had submitted that the authorizations / consent letters were filed but were not produced. The broker further submitted that all the clients whose accounts were adjusted with another were sister concerns. The submission of the broker on this issue is not satisfactory. The broker should not have mis-used client account by adjusting one account with another without proper authorization irrespective of the number of cases where it was done or the fact that all the clients were sister concerns.

4.1.5 Broker had not maintained separate ledger accounts with regard to transactions with associates as clients or others. The broker had submitted that a consolidated ledger of associate firms and companies was maintained as most of the time the transactions were of the nature of transfer of funds. Further, the broker submitted that the associate firms belong to the same owner hence, it was not felt necessary to maintain separate account. The broker has an obligation to maintain individual client accounts irrespective of the fact that all the clients are associates and belong to same owner. I find that the broker is guilty of not maintaining separate ledger account.

4.1.6 Broker had used clients' bank accounts for the purpose other than what is stipulated. The broker had submitted that Global Trust Bank had directly debited demat charges and bank guarantee commission to its account without an instruction from the broker. The broker further submitted that Global Trust Bank was instructed not to carry on such debits. However, the broker failed to produce any document to show such debits were credited back. I find that there were only 11 transactions of small amount and in only one bank i.e., Global Trust Bank.

4.1.7 Broker had not collected margins from his clients. The broker has submitted that the margin amounts were very small and all the clients were close relatives. Hence, he did not feel it was necessary to collect margins from clients. The broker further pointed out that there has been no default on the part of his clients. The margin amounts being very small or the clients being close relatives are no grounds for not collecting margins and as such the broker is guilty of not collecting margins.

4.1.8 Broker had passed of entries only after inspection commenced. Broker submitted that he mainly deals with arbitrage business and had opened the trading account in their books of accounts. Further, there was no sauda outside the book hence, no requirement of passing entries after inspection commenced. Broker contended that it did not require passing any entry in the books as all the entries and accounts are automated and done by the computers and as such the question of passing entries at the time of inspection does not arise. As observed by the Enquiry Officer there were no details given in the inspection report therefore, the submissions of the broker are accepted.

4.1.9 Broker had not made provision for tax, for interim period from 01.04.2000 to 30.09.2000. The broker had submitted it was a partnership firm and there is no requirement to make a provision for tax for half year. The broker also produced copies of TDS certificate for the year 1999-2000 and tax audit certificate for the year 1999-2000. I find there is no violation on part of the broker on the count of not making a provision for tax.

4.1.10 Broker failed to obtain confirmations from banks, creditors and debtors. The broker stated that there was no such requirement and contended that he was not asked for such confirmation during the inspection. However, the broker produced a copy of bank confirmation certificate from Janata Sahakari Bank and Global Trust Bank and a copy of tax audit report. In view of the documents produced by the brokers i.e., bank confirmation certificate and tax audit report I do not find violation on the part of broker.

4.1.11 Broker failed to time stamp the order slips and the order time was not reflected on the contract note. The broker submitted that 99% of the trades were in his proprietary account and do not require time stamping. Further broker contended that NSE format of contract note did not contain a provision of time stamp. I note that Enquiry Officer had examined a specimen contract note of NSE and

found that the specimen did not contain provision to mention order time. Enquiry Officer while agreeing with the submission of the broker felt it was a regulatory overlap and benefit of doubt be given to the broker. I agree with the Enquiry Officer.

4.1.12 Broker did not issue contract notes within the specified time. The broker stated that they had issued contract notes within 24 hours and there was not a single instance where contract note was not issued within specified time. Enquiry Officer observed that no instance of absence of acknowledgments were cited in the inspection report and as such benefit of doubt was given to the broker. I agree with the Enquiry Officer.

4.1.13 Broker did not have client registration forms completed and supporting documents were not in place for direct clients, the broker stated that client trades were less than 1%, so one proof of identity might have been obtained instead of two. Further, broker submitted that some clients have traded only once a year and in such cases there might have been non-compliance. As observed by the Enquiry Officer, inspection report did not contain details of instances of such non-compliances and therefore, benefit of doubt is being given to broker.

4.1.14 Broker failed to maintain order book as required by SEBI Circular dated 11.02.1997. The broker stated that he had only done few trades for his client and that the clients placed their orders on-line or over telephone and expected immediate reply, hence, it was not practical to maintain order book before placing the order. The said circular requires broker to maintain record of time when the client makes the order and reflect the same in contract note along with the time of execution of the order. As noted by the Enquiry Officer, in the absence of clarity in the inspection report as to whether the broker failed to maintain a physical record or had no record at all, the allegation fails.

4.1.15 As regards the broker's failure to obtain agreement from 17 clients, the broker submitted that the inspection team had asked for sample broker constituent agreement. Therefore, only 6 agreements were shown during the inspection. Further, the broker had produced the rest of the agreements during Enquiry. As such there is substantial compliance on part of the broker.

4.1.16 Broker delayed in making payments of funds to clients. The broker submitted that he had obtained letters from his clients to retain their funds for future purchases. However, clients were informed in advance in case of requirement of funds. In view of the consent letters obtained by the broker there is no violation on the part of the broker.

4.1.17 Broker had delayed in delivery of securities. The broker submitted that he had obtained consent from clients to keep securities for further sale. In other cases, there were clients who did not have demat accounts, broker was forced to keep the securities. I note that Enquiry Officer observed that out of the three transactions of non-compliance, one instance was that of an employee of the broker and the other two are of sister concerns and felt that it is not an offence serious enough to consider it a violation.

4.1.18 Broker failed to maintain a compliant register. Broker submitted that register was being maintained but there were no unresolved complaints. In the absence of any specific charge of unresolved complaints by the broker, Enquiry Officer recommended to drop the charge. I agree with this.

4.1.19 Gross exposure of broker was in excess of networth. The broker stated that gross exposure is monitored by NSE on daily basis and the terminal is deactivated the moment exposure exceeds the prescribed limit. In view of the terminal getting deactivated automatically once exposure limit is exceeded, broker is being given benefit of doubt.

4.1.20 Broker has deficit in terms of capital adequacy in networth. The broker stated that securities in the form of fixed deposits in banks, deposits with NSE were not included by the inspection team. NSE's prescribed format for computing the networth was strictly followed. The submission of the broker is accepted.

4.1.21 Broker traded on BSE and outside NEAT system, the broker stated that they have purchased and sold shares on BSE through a Registered Broker. Enquiry Officer observed that these transactions were done for broker himself and not for the clients and as such do not amount to off market transactions nor is there a need to issue contract notes. I agree with the Enquiry Officer.

4.1.22 With regard to the broker delaying in submitting audited balance sheet and profit and loss account for the year ended 31.03.2000 to the stock exchange, the broker had submitted that the last date to submit IT Return was extended by two months by the Government of India itself and delay in filing IT Return was only to that extent. Broker's submission is satisfactory hence accepted.

5.0 Order:

5.1 From the aforesaid discussion, I find that the irregularities committed by the broker are basically technical lapses and do not deserve a substantive punishment. I am accordingly inclined to accept the recommendation of the Enquiry Officer. Therefore, in exercise of powers conferred upon me in terms of Section 19 of the SEBI Act, 1992 read with regulation 13 (4) of SEBI (Procedure for holding Enquiry by Enquiry Officer and imposing penalty) Regulations, 2002 I hereby impose a minor penalty of warning on M/s. Bakliwal Investment and direct it to be more diligent in complying with the SEBI Act, Rules and Regulations framed there under. I also direct the broker to note that any instances of violations or non-compliance with the Act, Rules and Regulations in future shall be dealt with more stringently.

5.2 This order shall come into effect immediately.

Place: Mumbai

Date: 18th May 2004

A K Batra

Whole Time Member

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