

**SECURITIES AND EXCHANGE BOARD OF INDIA
ORDER**

UNDER REGULATION 13(4) OF THE SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002 AGAINST M/S MUNJAL LEASING LIMITED, MEMBER, NATIONAL STOCK EXCHANGE OF INDIA LIMITED, HAVING SEBI REGISTRATION NUMBER INB230837836.

1.0 FACTS OF THE CASE

- 1.1 M/s Munjal Leasing Limited (hereinafter referred to as “the said broker”) is a member of the National Stock Exchange of India Ltd. (hereinafter referred to as “NSE”) and a stock broker registered with the Securities and Exchange Board of India (hereinafter referred to as “SEBI”) under certificate of registration No.INB230837836.
- 1.2 Inspection of the books of accounts and other records of the broker was carried out by SEBI in the first week of July 2001 and the inspection related to the activities of the member-broker for the years 1998-1999, 1999-2000 and 2000-2001 (till the date of the inspection). In the course of the inspection, the following violations were observed:
- (a) Non-production of sauda book for the period 15.9.1998 to 21.10.1998.
 - (b) Irregularities in issuance of Contract notes:

- The contract notes did not bear pre-printed serial numbers.
 - Contract notes did not bear acknowledgement from clients.
 - Some contract notes were missing.
- (c) Dealing with unregistered sub-brokers.
 - (d) Non-segregation of own account and clients accounts.
 - (e) Submission of wrong information to SEBI.
 - (f) Non-redressal of investor grievances.

1.3 A copy of the inspection report was forwarded to the broker for his comments. The response of the broker was found to be unsatisfactory. Hence, an enquiry officer was appointed by SEBI, vide order dated 22.1.2003, to conduct an enquiry, as per the provisions of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as "Enquiry Regulations").

2.0 ENQUIRY PROCEEDINGS

2.1 The enquiry officer issued a show cause notice to the said broker, vide letter dated March 10, 2003, under Regulation 6 of the Enquiry Regulations, delineating the violations alleged to have been committed by them and advised them to show cause as to why appropriate penalty should not be levied on them for the said violations. A personal hearing was also offered before the enquiry officer on April 21, 2003. The date for hearing was rescheduled to May 26, 2003, at the request of the broker. Shri Sanjay Munjal, Director of the said broker, appeared before the enquiry officer and made submissions on May 26, 2003.

- 2.2 The enquiry officer, after considering the submissions made by the said broker, submitted her report on July 10, 2003, with the recommendation that a major penalty of suspension of certificate of registration for a period of 6 months may be imposed on the said broker.

3.0 SHOW CAUSE NOTICE AND PERSONAL HEARING

- 3.1 In view of the recommendation made by the Enquiry Officer, a show cause notice dated July 29, 2003 was issued to the said broker, advising them to show cause as to why appropriate penalty, including penalty as recommended by the Enquiry Officer, should not be imposed on them. The said broker sought an extension of time for one and half months for submission of detailed reply. This request was acceded to, by SEBI, and time was granted till September 30, 2003 for submission of reply to the show cause notice.
- 3.2 The said broker submitted their reply to the show cause notice, vide letter dated October 29, 2003. In their reply the said broker submitted as under:
- (a) They had resigned from the trading membership of NSE in May 2002 and have not operated their trading terminal since July 2001. They have also applied for cancellation of registration with SEBI, in May 2002. Therefore, the procedure laid down in Chapter III for summary procedure should have been followed.
 - (b) The inspection took place in July 2001 and the enquiry officer was appointed in January 2003. The enquiry officer did not have a copy of their comments on the findings in the inspection report.
 - (c) The enquiry officer has not included in her report, documents and explanations submitted before her; rather, she has made inferences on the basis of earlier records.

- (d) It is apparent from the copy of the proceedings before the enquiry officer that the original copy of the sauda book for the period 15.9.1998 to 21.10.1998 was produced before the enquiry officer; inspite of this, the enquiry officer has inferred that the sauda book has not been produced before the inspecting authority.
- (e) The contract notes for the period 2.9.1998 to 8.9.1998, which were stated to be missing by the inspection team, were submitted before the enquiry officer and the same were perused by her. However, in the report she has not made a mention regarding this and rather inferred that the said contract notes were not offered to be shown by them, in their comments on the findings in the inspection report.
- (f) The three entities viz. LRM Securities, Munjal Online Stock Access and the said broker are registered with SEBI and are members of DSE, OTCEI and NSE and hence they have not dealt with any unregistered brokers.
- (g) They have maintained separate bank accounts as per the requirement but there were stray cases where cheques may have been issued on account of error on the part of the accountant.
- (h) They have not furnished any wrong information to SEBI. What they meant was that they did not have any clients from July 2001 and their trading terminals were inoperative from February 2001.
- (i) In respect of non-redressal of complaint by R.C. Sardana, the said matter was considered by the enquiry officer in the enquiry against Munjal Online Stock Access and therefore this cannot be considered as a violation by them.

3.3 An opportunity of personal hearing was granted to the said broker on November 18, 2003. The said broker appeared before me and made further submissions. Subsequently, the said broker also furnished written submissions vide letter dated November 30, 2003, reiterating the submissions made during the hearing before me.

4.0 **CONSIDERATION OF ISSUES**

4.1 I have taken into consideration the facts and circumstances of the case, the material available on record, including the show cause notices issued to the said broker, the enquiry report, the submissions made by them in reply to the notices and during the hearings and all the documents furnished by them. My findings on the allegations made against the member-broker are as follows :

4.2 **Absence of pre-printed serial numbers on the contract notes**

4.2.1 Regarding the allegation that the contract notes did not have pre-printed serial numbers, I note that the said broker has admitted that their contract notes did not bear pre-printed serial numbers, but the numbers were generated on a day to day basis, by their back office software. I agree with the findings of the Enquiry Officer that computer generated serial numbers are also acceptable, provided they run continuously from the first day till the last day of the financial year. In the absence of such a system of numbering contract notes, it would be possible for the brokers to insert back dated contract notes or to take out contract notes, for the period at the end of each settlement. In order to avert the possibility of such manipulations by brokers, SEBI had, vide circular dated August 05, 1996, directed all stock brokers to ensure continuous numbering of contract notes. Therefore, I find that the said broker has violated the provisions of the said circular.

4.3 **Missing contract notes**

4.3.1 The enquiry officer has found that the inspection team had made the observation regarding missing contract notes, on the basis of random sampling and thus there is a possibility that the said broker was not

regularly issuing contract notes to his clients. In this regard, I note that during the enquiry proceedings held on 26.5.2003, the director of the said broker had stated that he was going to produce the missing contract notes on the next date of hearing. He has subsequently forwarded a copy of a letter dated 29.5.2003, purportedly making written submissions before the enquiry officer. In the said letter it was mentioned that the missing contract notes were produced. However, copies of the said contract notes were neither enclosed with any of the several letters sent to SEBI subsequently nor have they been produced before me. In view of the above, I find that there is no proof that these contract notes were actually produced before the enquiry officer. In the absence of submission of any proof by the broker, regarding having issued these contract notes, I tend to agree with the finding of the enquiry officer that there is a pre-ponderance of probability that the said broker had not been issuing contract notes to some clients.

4.4 Acknowledgements not obtained from clients, for contract notes issued

- 4.4.1 I note that the said broker has failed to obtain acknowledgement from clients in several instances. In this regard, the said broker has not made any submissions, in his reply to the show cause notice or in the course of personal hearing. The said broker has submitted before the enquiry officer that in the case of outstation clients, contract notes were sent by post and hence, it was not possible to obtain acknowledgements from those clients. I am unable to accept the explanation of the said broker and tend to agree with the finding of the enquiry officer that the said broker could have produced documents such as acknowledgements (in case of Regd. Post) or UPC slips etc, to prove despatch of the contract notes. I note that the broker failed to bring on record any other proof of having delivered the contract notes in time, to the respective clients, either during the Enquiry proceedings or subsequently. Therefore, I

concur with the findings of the Enquiry Officer that the said broker has failed to obtain valid acknowledgements in respect of contract notes issued by them and has therefore violated the provisions of SEBI Circulars dated 18.11.1993 and 5.8.1996.

4.5 Non segregation of own accounts and client accounts

4.5.1 I note from the inspection report that the said broker has failed to maintain a clear distinction between his own account and the client account. The inspection report has highlighted several instances where funds have been utilised from the client's account to meet administrative expenses such as hire purchase charges, salary and wages, printing and stationary, insurance charges etc. There has also been a transfer of funds from the client's account to the broker's own account. In their reply, the said broker had submitted that it was possible that there were a few cases where cheques were wrongly issued by the accountant from the client's account. Thus, I find that the said broker has admitted to utilising funds from the client's account for administrative and other purposes, unrelated to clients' activities. SEBI, vide its circular dated November 18, 1993, had clearly stated the use of the "client account" as well as the kind of deposits/withdrawals that could be made into/out of the account. This was done to clearly segregate the clients' funds from that of the broker's. Use of the client account for purposes other than those mentioned in the said circular leave the client account vulnerable to mis-utilisation. I find that the said broker has failed to maintain the required segregation between the clients' funds and his own. Thus, he has failed to comply with the directives of SEBI Circulars dated 11.11.93 and 5.8.1996.

4.6 Dealing with un-registered sub brokers

4.6.1 I note that the said broker has dealt with Munjal Online Stock Access, Dealer, OTCEI and LRM Securities Ltd., Member, DSE, allowing them to

act as their sub-brokers. In this regard, the said broker has submitted that they have not dealt with any un-registered brokers. They have also submitted that LRM Securities and Munjal Online Stock Excess were both member/dealers of DSE and OTCEI, respectively and were also registered with SEBI in these capacities. Moreover, these firms were also their associate concerns. Hence, clients of these firms, who wanted to carry out transactions at the NSE, would place orders with them and there was nothing wrong in the said transactions. Thus, the said broker has admitted that they were allowing the clients of their associate firms to trade on NSE.

- 4.6.2 In view of the above, I agree with the enquiry officer that though both the firms were registered with SEBI as brokers of DSE/OTCEI, they were not acting in their capacity as brokers. They were routing the transactions of their clients through NSE, thereby acting as sub-brokers of the said broker. Thus, the act of the said broker, in allowing the transactions of the clients of the aforesaid firms, to be routed through NSE, amounts to dealing with unregistered sub brokers. Therefore, I find that the said broker has acted in violation of the directives of SEBI, issued vide circulars dated 14.3.1996, 31.3.1997 and 16.1.1998.

4.7 **Non maintenance of books of accounts**

- 4.7.1 I note from the inspection report and the report of the Enquiry Officer that the said broker had failed to produce the sauda book for the period 15.9.1998 to 21.10.1998, before the inspecting officials. In this regard, the said broker had submitted that he had produced the same before the Enquiry Officer, which she verified to her satisfaction. In the circumstances, I find that although the said broker cannot be held guilty of having failed to maintain the sauda book, he did not co-operate with the inspecting officials and failed to produce records sought for, by them.

4.8 Submission of wrong information to SEBI

4.8.1 I note from the inspection report that when the said broker was asked to submit details of active clients and the top 20 clients in terms of turnover, they had submitted that they had no clients. However, the names of 6 clients were obtained by the inspecting officials from the client commitment report for the period 7.2.2001 to 20.2.2001. In this regard, the said broker had submitted that their trading terminal was not operative from February 2001 and the clients mentioned in the inspection report were old clients who could have done an odd trade each. They further submitted that they had no intention to give wrong information to SEBI. I find the explanation of the said broker to be unsatisfactory. I note that there were indeed clients being serviced by the said broker, during the period relating to which information was sought by the inspecting officials. They should have provided the names of their clients to SEBI, irrespective of the number of trades being done by such clients. Therefore, I find that by not providing the information sought for and by denying the existence of any clients, the said broker is guilty of having submitted wrong information to SEBI.

4.9 Non-redressal of investor grievances

4.9.1 I note that a complaint by Shri R.C. Sardana is yet to be redressed by the said broker. In this regard, I note that the complaint of Shri R.C. Sardana is a subject matter of arbitration before the Delhi Stock Exchange and an arbitration award has also been passed on 30.7.2003. Therefore, I grant a benefit of doubt to the said broker.

4.10 Other issues

4.10.1 The said broker has contended that since he had made an application for surrender of registration, the procedure laid down in Chapter III, rather than the procedure in Chapter II of the Enquiry Regulations, should have been followed. In this regard, I note that the present proceedings have

initiated for violations of the SEBI (Stock-Brokers and Sub-Brokers) Rules and Regulations, 1992, SEBI Act, 1992 etc. Any penalty for violations of the Act, Rules or Regulations by a Stock Broker can be imposed only pursuant to proceedings under Chapter II of the Enquiry Regulations.

4.10.2 Further, the application for surrender of registration has been made by the said broker in May 2002, much after the violations had taken place and also after they were called upon to furnish their comments on the findings of SEBI inspection. The application for surrender thus appears to be a device to avoid penalty for the violations committed by them. In view of the above, I find that there is no merit in the contention of the said broker and that the present proceedings have rightly been initiated under Chapter II of the Enquiry Regulations.

4.11 It is clear from the above that the said broker has

- i. failed to comply with several requirements in respect of issue of contract notes,
- ii. failed to maintain proper segregation between clients' funds and own funds,
- iii. dealt with unregistered sub-brokers, and
- iv. submitted wrong information to SEBI.

4.12 In view of the above, I concur with the recommendation of the Enquiry Officer that a suitable penalty ought to be levied on the said broker, for having violated the various regulatory requirements. I have also noted from the arguments put forth by the said broker, in response to the allegations made against them, that they have poor knowledge of the regulatory requirements with respect to a registered broker e.g. they seem to be unaware of the fact that a broker of one exchange, in case he wishes to execute his clients' transactions through the broker of another

exchange, needs to get himself registered as a sub-broker of the latter. In addition, the said broker displays a casual approach towards compliance requirements, evident from their replies, attributing non-segregation of client/own account to “a few instances”, “accountant’s error” etc, as also the fact that the said broker had submitted wrong/inadequate information to SEBI, despite specific queries.

- 4.13 Accordingly, in view of the facts and circumstances of the case, I find that that the penalty of suspension of registration for a period of 6 months recommended by the Enquiry Officer is justified.

5.0 **ORDER**

Therefore, I, in exercise of the powers conferred on me in terms of Section 19 of the SEBI Act, 1992, read with regulation 13 (4) of the Enquiry Regulations, hereby suspend the certificate of registration bearing No. INB230837836, granted to M/s Munjal Leasing Limited, for a period of six months. This Order shall come into effect on the expiry of 21 days from the date of this Order.

A.K.BATRA

PLACE : MUMBAI

WHOLE TIME MEMBER

DATE : June 9th , 2004 SECURITIES AND EXCHANGE BOARD OF INDIA