

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 SAIKALA ASSOCIATES PVT.LTD, AFFILIATED TO M/S.HSE SECURITIES LTD, MEMBER OF NATIONAL STOCK EXCHANGE, WITH SEBI REGISTRATION NUMBER INS230854734.

CO/ /MIRSD/ /04

1. Saikala Associates Pvt.Ltd is a sub-broker (hereinafter called as “the sub-broker”) affiliated to M/s.HSE Securities Ltd a member of National Stock Exchange (hereinafter called as “NSE”) and registered with the Securities and Exchange Board of India (hereinafter referred to as “SEBI”) under certificate of registration number INS230854734. The sub-broker has its office at D.NO.1-8-468, Laxmi Bhavan, Chikkadpally, Hyderabad -500 020.
2. SEBI conducted inspection of the sub-broker of its books of accounts, documents and other records on May 30, 2002 for a period of 2 years from the year 2000 till the date of inspection, where certain irregularities were noticed.
3. An enquiry officer was therefore appointed vide order dated 21.11.03 under SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulation 2002, to enquire into the affairs and dealings of the broker for finding out the possible violations of the following provisions of law :
 - a) Section 12 of SEBI Act,1992
 - b) SEBI Circular No.SMD/POLICY/CIR-3/98 dated 16/01/98
 - c) SEBI Circular No.SMD/POLICY/CIR-32/99 dated 14/09/99
 - d) SEBI Circular No.SMD/POLICY/CIR-33/2000 dated 27/07/00
 - e) SEBI Circular No.SMD/POLICY/CIR-12/2000 dated 17/05/02
 - f) SEBI Circular No. SMD/ SED/CIR- 93/23321 dated 18/11/93
 - g) SEBI Circular No.SMD/POLICY/CIR-11/1997 dated 21/05/97
 - h) Regulations 15 read with code of conduct as specified in schedule II of the SEBI (stock-broker and sub-broker) Regulations, 1992.
 - i) Bye laws, Rules and Regulations of Stock Exchange
4. After conducting enquiry as per enquiry regulations, the Enquiry officer submitted his report on 19.05.2004 and found that the sub-broker violated the provisions of SEBI Act, Rules And Regulation made there under and recommended a penalty of suspension of registration of the broker for a period of one month for violation of the Rule 3 of SEBI (Stock Brokers & Sub-Brokers) Rules, and Section 12 of the

SEBI Act 1992 and a warning be issued for the remaining violations as mentioned above.

5. A show cause notice dated 26.05.2004 under regulation 13(2) of Enquiry Regulations was sent asking the sub-broker, to show cause as to why the penalty as recommended by enquiry officer should not be imposed.
6. The sub-broker vide letter dated 07.06.2004 replied to the said show cause notice and made submissions as follows regarding the aspect of acting as a sub broker:
 - ✍ The sub-broker stated that during the year 2000 when they started trading through M/s. PCS Securities Ltd, they submitted an application for registration as a sub broker to M/s. PCS Securities Ltd for onward transmission to NSE and SEBI. The sub-broker stated that, a demand draft for Rs.1,000 (Rupees One Thousand) vide DD No.825824/2000 dt.18.7.2000 drawn on The Vysya Bank Ltd towards SEBI registration fee was also enclosed to the said application. The sub-broker further stated that M/s. P.C.S. Securities Ltd had informed them that the application had been forwarded to the NSE for registration.
 - ✍ The sub-broker stated that, they had made all the payments to their clients promptly and well within time. The sub-broker stated that they had also kept their commitments and had never defaulted either to the exchange or to their clients / investors. The sub-broker stated that high priority was always given in honoring commitments to the investors and that the investors were never put to any loss. He further stated that at no point of time they had failed in meeting their obligations towards payments / deliveries to the clients. The sub-broker stated that majority of their clients who had started business with them in the year 2000 were still continuing with them. It was also stated that they never acted prejudicial to the interest of the investors / clients.
 - ✍ The sub-broker stated that they had maintained scrupulous track record in meeting their statutory obligations as per the law. The sub-broker stated that they paid heavy amounts towards Income Tax, Service Tax and SEBI turnover fee and furnished the same in a tabular form as under :

Financial Year	SEBI Turnover Fee Amt Rs.	Amount of Income Tax paid : Amt. Rs.	Amount of Service tax paid to Govt. Amt. Rs.
1998-1999	5,000.00	2,50,760.00	89,193.81
1999-2000	11,377.00	8,53,329.00	3,67,252.79
2000-2001	18,314.92	5,50,928.00	2,47,383.00
2001-2002	61,218.80	3,19,151.00	1,35,653.50
2002-2003	5,000.00	1,01,418.00	1,01,221.96
2003-2004	N.A.	2,00,000.00 (Advance Tax)	2,62,515.00
Up to May'2004	N.A.	N.A.	61,720.00
Totals	1,08,910.72	22,75,857.00	12,64,939.98

- ✍ The sub-broker stated that the above indicated their promptness in discharging their duties. The sub-broker submitted that, they paid such huge amounts towards taxes and kept up their commitments promptly, and stated that there was no question of failing to meet their statutory obligations towards investors. The sub-broker further stated that the concept of efficient, timely and effective service to the investors was their main strength that had made their clients to stay with them all along even in a highly competitive market environment.
- ✍ The sub-broker submitted that no prejudice / loss was caused to any of their clients / investors and requested to condone their lapse and pardon them.
- ✍ With regard to, inadequacy in maintenance of client database sub broker submitted that at the time of the inspection i.e., in May 2002, about 90% of their clients were registered with them and that they had their client agreements on record. The sub-broker stated that only in some isolated cases, where they made a single transaction, registration forms could not be traced.
- ✍ The sub-broker stated that, as on date all their clients had submitted their client registration forms / agreements and they were on record with complete details. The sub-broker stated that the client database as per SEBI Rules and Regulations were maintained and agreements with all the clients on the required stamp paper were entered into.
- ✍ With regard to Segregation of clients Funds from own funds, the sub-broker stated that their Pay-in / Pay-out Account was maintained with Canara Bank and that they also maintain a separate account with them for their client's funds. The sub-broker stated that they were maintaining a separate account with Canara Bank, HSE Branch so as to have clear-cut classification with regard to clients and own funds. The sub-broker stated that their Account with The Vysya bank Ltd is now being used only for the purpose of meeting their overheads out of the Brokerage Income received by them, being shifted on regular basis from their Pay-in/Pay-out account at Canara Bank, HSE Branch.
- ✍ The sub-broker contended that at no point of time they used clients' funds for own purpose as their funds in the account had always been much higher than that of clients. The sub-broker requested SEBI to condone the above lapse in light of complexities associated with nature of business and excuse them for this time.

- ✍ The sub-broker stated that the SEBI inspecting officials during their inspection made observations at their office on their good track record as there were
 - ? nil/no investor complaints, arbitration cases, bad deliveries, no disciplinary action initiated / pending against them
 - ? no violation on their part of the provisions of the sub broker agreement / bye laws etc., regarding trade restrictions and margin money
 - ? no default in settling payments / deliveries at any point of time either to the exchange or to their clients.
 The broker stated that these noting speak about their sincerity and commitment to their business and their respect for the laws of SEBI.
 - ✍ The sub-broker stated that suspension of their registration even for a brief period will cause undue hardship not only to them but also to their existing and long standing clients
 - ✍ The sub-broker stated that they would lose the existing clientele and would not get any new clients because of the dent in their image due to suspension. The sub-broker stated that it might have demoralizing effect on their organization and its personnel and stated that there was risk of losing the confidence of other market participants like HSE, HSES, NSE, their Bankers and their Depository.
7. I have gone through the inspection report, enquiry report, the show cause notice, the reply of the sub-broker and the material available on record and following are the findings on each of the allegations:

a). ACTING AS AN UNREGISTERED SUB BROKER

With regard to the charge that sub-broker acted as unregistered sub-broker of PCS Securities, the enquiry officer observed that the sub-broker admitted the violation and the reasons given by the sub broker justifying the said act are emotional and are not based on legal principles. The enquiry officer found that the provisions of Rule 3 of SEBI (Stock Brokers & Sub-brokers) Rules 1992, Section 12 of SEBI Act, 1992 and the Circulars issued there under clearly prohibit a person from acting as a sub-broker without holding a valid registration from SEBI and no exemption had been granted for members of Stock Exchanges in this regard. The enquiry officer observed that the evidences on record clearly establish that the member had acted as unregistered sub-broker to M/s PCS Securities Ltd., member – NSE, on behalf of his clients and that the sub – broker created volume of about Rs. 403.29 crore while acting as unregistered sub – broker which made the violation more serious. The enquiry officer observed that, the investors would not have recourse to NSE against the sub-broker, in the event of disputes arising out of the transaction, as the sub broker is not a registered sub-broker of the main broker of NSE and no confirmation memos/purchase/sale bill of the NSE member were issued to the investors. I agree with the finding of the enquiry officer that the sub broker was guilty of violating the provisions of Rule 3 of SEBI (Stock Brokers & Sub

Brokers) Rules, 1992, Section 12 of SEBI Act, 1992 and the Circulars issued by SEBI in this regard.

The sub-broker in his reply to the show cause notice dated 07/06/04 stated that during the year 2000 when they had started trading through M/s. PCS Securities Ltd, an application for registration of sub broker was submitted to them for onward transmission to NSE and SEBI. The sub-broker stated that together with the application a demand draft for Rs.1,000 (Rupees One Thousand) vide DD No.825824/2000 dt.18.7.2000 drawn on The Vysya Bank Ltd towards SEBI registration fee was also enclosed. The sub-broker stated that M/s. P.C.S. Securities Ltd informed them that they had forwarded their application to NSE membership department for the purpose of registration. The sub-broker enclosed the copies of letter of application and Xerox copy of DD for reference. Acting as an unregistered sub-broker is not permitted under SEBI (stock broker and sub-broker) Rules even during pendency of registration.

The sub-broker has simply reiterated what was stated before the Enquiry officer and therefore, I agree with the finding of the enquiry officer and hold the sub-broker guilty of violation stated above.

b). INADEQUACY IN MAINTENANCE OF CLIENTS DATABASE

The enquiry officer found that the sub-broker did not maintain the Client registration forms for some of the clients. I note that the sub-broker in his reply to the show cause notice has stated that in May 2002, about 90% of the clients transacting on regular basis were registered with them and had their client agreements on record. The sub-broker further stated that only in some isolated cases, where they have made a single transaction registration forms could not be traced. The sub-broker stated that as on date all their clients have submitted their client registration forms/agreements to us and that they are on record with complete details. The enquiry officer stated that the circular does not distinguish between clients with frequent trading and infrequent trading/one time trading. The inspection team observed that the sub-broker did not have registration forms for about forty clients and it was further observed that when the sub – broker was asked about few specific cases, he failed to furnish the agreement with his clients. These cases are as follows:-

NAME	CODE NO.
G.Ansuya	A057
Alluriah	A058
T.Chandramohan	C019
P.Gopal Reddy	G022

I therefore agree with the finding of the enquiry officer that the sub broker is guilty of violating the circular no. SMD/POLICY/OECG/1-97 dated 11.2.97 for their failure to enter into an agreement with clients.

c). NON SEGREGATION OF CLIENTS FUNDS FROM OWN FUNDS

The enquiry officer found that the sub-broker did not segregate the client's funds from his own funds and operated only a common bank account for both clients and for self.

I note that the sub-broker in his reply to the show cause notice stated that their pay-in / pay-out account was maintained with Canara Bank and also had separate accounts with them for their clients' funds. The sub-broker stated that they were using their account with Vysya Bank as the account for their clients due to operational convenience and the same account was also used to meet their establishment expenses like salaries, electricity and etc since they were also enjoying the over draft facility with Vysya Bank against their Fixed Deposits. The sub-broker contended that after getting the SEBI Sub – Broker Registration under HSE Securities Ltd in January 2001 they had been maintaining a separate account with Canara Bank (HSE Branch) so as to have clear – cut classification with regard to clients and own funds. The sub-broker stated that their account with Vysya Bank at present is used only for the purpose of meeting their overheads out of the Brokerage Income received by them. The sub-broker further stated that at no point of time they used clients' funds for own purpose as their funds in the account were much higher than the clients' funds.

The enquiry officer found that the sub-broker admitted the violation of retaining the funds of the clients for a longer period without their consent. I agree with the finding of the enquiry officer that although the sub – broker had now started maintaining a separate account with Canara Bank, he had certainly failed to comply with the requirement of having a separate bank account for clients so as to segregate the clients funds from own funds and the said act is in violation of SEBI circular No. SMD/SED/Cir/93/23321 dated 18.11.93.

8. I have noted that the enquiry officer found the sub-broker not guilty of following charges:
 - ✍ Non-reporting of off- the floor transactions
 - ✍ Non-maintenance of books of accounts and records
 - ✍ Non-maintenance of deposit of minimum margin by clients
 - ✍ Delay in delivery/payment to clients.
9. Upon considering all the facts of the case, I agree with the findings of the Enquiry Officer that most of the violations are technical in nature but the violation of dealing as unregistered sub-broker and non segregation of clients' funds from own funds are serious in nature, since the interest of investors at large is involved. I therefore agree with the recommendation of the enquiry officer for imposing a minor penalty of suspension of registration.

10. Therefore, in exercise of the powers conferred upon me by Section 4(3) of SEBI Act, 1992 read with Regulation 13(4) of the Enquiry Regulations, I hereby suspend the certificate of registration bearing INS230854734 granted to Saikala Associates Pvt. Ltd for a period of one month. This order shall come into force on expiry of three weeks from the date of order.

Date : 27/12/2004

Place : MUMBAI

**G.N.BAJPAI
CHAIRMAN
SECURITIES AND EXCHANGE BOARD OF INDIA**