

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

Order under Section 11(1) and Section 11(4)(d), read with Section 11B and Section 19 of the SEBI Act, 1992 in the matter of (1) M/s Digital Stocks & its Proprietor, Shri Dheeraj Kumar Madaan, (2) Ganpati Finsec Pvt Ltd and its directors Shri Devender Mittal, Smt. Ritu Mittal and Dr. K.C Mittal

1.0 Background

1.1 SEBI received a complaint dated 28.8.2005 from Abohar Investor Forum (hereinafter referred to as AIF) from Abohar, District Ferozepur, Punjab alleging the following:

- misappropriation of shares and funds of small investors by one Shri Dheeraj Kumar Madaan (hereinafter referred to as DKM), Proprietor of M/s Digital Stocks, having its address at 3, Circular Road, Mawa Market, Abohar, District Ferozepur (Punjab).
- that DKM was an associate of M/s Ganpati Finsec P. Ltd., who was a sub-broker of SAM Global Securities Ltd. (member BSE).
- that DKM had absconded on 30th June 2005 with investors' money.

1.2 AIF further informed that it had contacted Ganpati Finsec P. Ltd (GFPL) and SAM Global Securities Ltd. for redressal of investors' grievances, however no action had been taken by them. Meanwhile, SEBI also received another complaint dated 20.8.2005 from one Smt. Santosh Kumari (an Abohar based investor) alleging that DKM had absconded with her money/ shares. She also provided a statement of account stated to have been issued by Digital Stocks. Earlier, AIF had named Smt. Santosh Kumari also as an investor registered with it. Additionally, there were widespread media reports highlighting the fact that DKM had run away with huge money/ shares of investors.

1.3 The allegations made in the complaints were examined by SEBI. The representatives of AIF were called to the Northern Regional Office of SEBI at Delhi on 05.09.05 and 12.09.05 for further inquiries and information. A statement of AIF's president Sh. P.N. Sehgal was recorded on 12.9.2005. The comments of the brokers SAM Global Securities Ltd., member BSE (hereinafter referred to as SAM), SMC Global Securities. Ltd., member NSE (hereinafter referred to as SMC) and their franchisee GFPL have also been obtained. A statement of Shri Rakesh Gupta, representative of the said brokers was also recorded on 13.09.05 and 14.09.05. Independent enquiries were also made with Ludhiana Stock Exchange, Stock Holding Corporation of India Ltd. (SHCIL) Mumbai and India Bulls Securities Ltd., New Delhi. (hereinafter referred to as India Bulls). A preliminary investigation into the matter was conducted. The findings of the preliminary investigation are given below.

2.0 PRELIMINARY FINDINGS

2.1. The enquiries made by SEBI prima-facie revealed the following:-

- SMC claims to have its branch office at Abohar. SMC has further informed that it had entrusted the management of its said branch to its franchisee viz. GFPL, who is based in Sri Ganganagar, Rajasthan. GFPL in turn appointed DKM as the sub agent for managing SMC's so-called branch at Abohar.
- DKM was managing SMC's so-called branch at Abohar for around 3 years.
- DKM was neither an employee of GFPL nor of SMC.
- DKM was trading for a large number of Abohar based investors. DKM was not putting client codes on the terminals and all the orders by various Abohar based clients were placed in common client code i.e. 99G606, which is of GFPL.
- DKM had without informing his investors, closed his establishment and run away on 30th June 2005 with the money/ shares of various investors. He alongwith his wife are reportedly untraceable till date.
- The investors thereafter formed an association in the name of "Abohar Investors Forum" to get their dues. AIF had initially contacted Shri Devender Mittal of GFPL, Ganganagar, but he refused to acknowledge investors' claim.
- AIF's representative also contacted SAM vide letter dated 20.7.2005. However it was only after SEBI's intervention that SAM replied to AIF vide its letter dated 1.9.2005. SAM's representative also visited Abohar on 8th September 2005 and received claims of aggrieved investors.
- SMC has subsequently informed that it had suspended all the trading IDs of its NSE terminals located in Abohar. Further, SAM had informed that it had frozen the demat account of DKM with it.
- After DKM became untraceable, AIF had advertised in local newspaper asking investors to register with AIF. 59 investors have made a claim of around Rs. 50 lacs with AIF.

2.2. Preliminary inquiries made by SEBI revealed that DKM/ Digital Stocks have the following demat accounts:

Sl. No.	DP beneficiary account no.	DP Code	Depository	DP name
1	10170216	IN 302236	NSDL	India Bulls Securities Ltd.
2	1201911100006275	-	CDSL	SAM Global Securities Ltd.
3	1601010000026460	-	CDSL	Stock Holding Corp. of India Ltd.

It further emerged that despite the reports that DKM had run away with investors' funds/shares on 30.6.2005, he continued to be actively involved in securities business, as is apparent from the following -

- Transaction statement with SHCIL showed that DKM had transferred some shares from his DP account on 12/13.9.2005. It has been learnt that these transfers were executed from Chandigarh and Jaipur branches of SHCIL, apparently indicating that DKM was operating from these cities on the said dates. All the transfers were made to his DP account maintained with India Bulls.
- It has been learnt from India Bulls that M/s Digital Stocks has been actively trading in securities through their internet module even after DKM made himself scarce to avoid the heat. As on 16.9.2005, it is noted that Digital Stocks had credit balance of Rs. 3.25 lacs with India Bulls.

2.3. Meanwhile, AIF has vide its certificate dated 30.09.2005 confirmed that all the claims of investors have been taken over by GFPL and GFPL has also made payment to all claimants registered with AIF.

3.0. VIOLATIONS BY DKM

3.1. Acting As Unregistered Sub-Broker

As may be seen from the information and details gathered and enquiries from AIF, GFPL, SMC & SAM, from the claim submitted by AIF and clients, members and also from DP accounts, DKM was dealing on behalf of various clients based in Abohar. All the orders on behalf of clients were placed by DKM in the client code of GFPL. These clients were not registered with SMC/SAM. DKM was issuing his own account statements to the clients on his own for their dealings in shares, though done through SMC/SAM. As informed by AIF, for their dealings in shares, all the cheques were issued by investors in favour of Digital Stocks and payment was also received by them from Digital Stocks. It was further informed by AIF that all shares sold by their investors were transferred to the DP account of DKM and similarly deliveries were received by them from the DP account of DKM.

DKM is not registered with SEBI as a sub-broker. As per section 12(1) of SEBI Act "*No stock broker, sub-broker----- and such other intermediary who may be associated with securities market shall buy, sell or deal in securities except under and in accordance with the conditions of a certificate of registration obtained from the Board in accordance with the regulations made under this Act.*"

As per Rule 3 of SEBI (Stockbroker and Sub-brokers) Rules, 1992 "*No stock broker and sub-broker shall buy, sell, deal in securities, unless he holds a certificate granted by the Board under the regulation.*"

The dealings by DKM as an unregistered sub-broker is prima facie in violation of section 12(1) of SEBI Act, 1992 and Rule 3 of SEBI (Stockbroker and Sub Brokers) Rules, 1992.

3.2. Defrauding Small Investors

As gathered from media reports, statements/ submissions made by AIF & SMC/SAM, DKM had run away from Abohar without informing his clients who were dealing through him in securities with their funds and securities. As per the claims submitted by various investors to AIF, he owed approx. Rs. 50 lacs to 59 investors. This prima-facie shows that DKM defrauded small investors of their money & shares, which is a violation of Regulations 3(a), 3(c) & 4(1) of SEBI (Prohibition of Fraudulent & Unfair Trade Practices Relating to Securities Market) Regulations, 2003, which read as follows:-

"Prohibition of certain dealings in securities

3. No person shall directly or indirectly—

(a) buy, sell or otherwise deal in securities in a fraudulent manner;

(c) employ any device, scheme or artifice to defraud in connection with dealing in or issue of securities which are listed or proposed to be listed on a recognized stock exchange;

4. Prohibition of manipulative, fraudulent and unfair trade practices

(1) Without prejudice to the provisions of regulation 3, no person shall indulge in a fraudulent or an unfair trade practice in securities."

4.0 VIOLATIONS BY GFPL

4.1. Acting As Unregistered Sub-Broker

As informed by AIF, GFPL was placing all the orders for purchase/ sale of shares on behalf of Abohar based clients in its own code through DKM. None of these clients was registered with SMC/SAM and no contract notes were ever issued to them by SMC/SAM.

Shri Rakesh Gupta, director of SAM/SMC admitted that almost all the trades reported from their Abohar branch were in the account of GFPL, who in turn was trading for various unregistered clients.

A perusal of data provided by clients and DP account statements of DKM shows that shares/ funds of clients were not transferred to account of SMC. Instead, all shares/funds were collected by DKM who, in turn, transferred them to the account of GFPL, who, in turn, passed them as its own in dealing with SMC/SAM.

However, it is noted that GFPL was not registered with SEBI as a sub-broker. Hence, GFPL was acting as unregistered sub-broker in violation of section 12(1) of SEBI Act and Rule 3 of SEBI (Stockbrokers and Sub brokers) Rules, 1992.

5.0 VIOLATION BY SMC GLOBAL SECURITIES LTD /SAM GLOBAL SECURITIES

5.1 Illegal Distribution of terminals:

As per SEBI circular no. SMDRP/Policy/Cir/49/2001 dated 22.10.01, the member should not give trading terminals at places other than registered office, branch office or registered sub-broker offices. It was prima facie seen that:

- a. SMC/SAM has installed their terminals at various places in and around Sri Ganganagar (including Abohar). SMC/ SAM have a franchise agreement with GFPL, Specifically for Sri Ganganagar location. Their terminals at other places were also being managed by GFPL as per the admission of SMC/SAM
- b. The said locations where terminals have been installed are referred as branches by SMC/SAM which is not only factually incorrect but also highly misleading. For any establishment to be called or treated as branch, it should prudently meet certain minimum requirements such as:
 - The establishment should carry on either the same or substantially the same activity as that carried on by the head office
 - The premises should be either owned or rented by same organisation.
 - The employees of branch office should be controlled from Head Office.
 - The branch should work in the same name as that of Head Office, i.e the branch (e.g GFPL or Digital Stock) should not have separate identity or name different from head office (SMC/SAM).
 - The profit/loss from branch should be reflected in consolidated accounts of Head Office. Even if branch is independent profit center, its profit / loss should be linked to consolidated accounts of organisation.

It appears that none of these conditions were fulfilled by the so-called branches or the Franchisee of SMC/SAM including GFPL and M/s Digital Stock. Apparently, these franchisees / locations are wrongly termed as branches in order to circumvent the provisions of SEBI circular no SMDRP/Policy/Cir/49/2001 dated 22.10.01. The said SEBI circular does not envisage location of terminals at places other than registered office, branch office or registered sub-broker offices. The terming of a franchise location as a branch does not actually make it branch and therefore the arrangement is illegal and in violation of the said SEBI circular.

In view of the above it appears SMC/ SAM has prima facie violated the provisions of the above mentioned SEBI circular.

6. 0. ORDER

Under the facts and circumstances as stated above, it is therefore incumbent upon the regulator to take emergent and remedial steps to safeguard the interests of the investors and the orderly development of the securities market.

While, the role of the brokers involved (SMC/SAM) is being examined separately, it is prima facie found that DKM even after running away with investor funds/shares on 30.06.2005 continues to be actively involved in securities business and is trading through internet module of India Bulls, therefore, by exercising powers under section 11(1), section 11(4)(d) read with section 11B and section 19 of the SEBI Act, in order to prevent the affairs of DKM and GFPL being conducted in a manner detrimental to the interests of the investors, in any manner whatsoever, pending completion of final proceedings, it is directed that:

- a. Shri Dheeraj Kumar Madaan, Proprietor of M/s Digital Stocks, having its office at 3, Circular Road, Mawa Market, Abohar, District Ferozepur (Punjab) is prohibited, with immediate effect, from buying, selling or dealing in securities or being associated with the securities market in any manner.
- b. GFPL and its directors namely Shri Devender Mittal, Smt. Ritu Mittal and Dr. K.C Mittal are prohibited, with immediate effect, from buying, selling or dealing in securities or being associated with the securities market in any manner whatsoever.
- c. NSDL/CDSL shall freeze, with immediate effect, all the demat accounts of Digital Stocks and its proprietor Shri Dheeraj Kumar Madaan, maintained with them.
- d. India Bulls Securities Ltd shall freeze, with immediate effect, the trading account of Digital Stocks and its proprietor Shri Dheeraj Kumar Madaan.
- e. Appropriate proceedings are being initiated against SMC Securities Ltd. and SAM Global Securities Ltd. for alleged irregularities in their franchisee operations. In the meantime, these brokers are directed to review their systems and procedures and confirm to SEBI within 15 days from the date of receipt of the order that all their operations are within the framework of SEBI regulations, rules and guidelines.

I am of the considered view that due to imminent urgency and in order to safeguard the integrity of the securities market, the previous notice to show cause can be dispensed with and it will be in the interest of justice to pass an ex-parte order. Any person aggrieved by this interim ex-parte order may approach SEBI within 30 days of this order showing cause for reconsideration of the directions.

The directions in this order will come into force with immediate effect.

Place: Mumbai

**WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA**