

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

AGAINST LIMRA SECURITIES LTD., MEMBER, NATIONAL STOCK EXCHANGE, SEBI REGISTRATION NO. INB230782430 UNDER REGULATION 13(4) SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002**1.0 BACKGROUND**

- 1.1 Limra Securities Ltd. (hereinafter referred to as the 'broker') is a member of the National Stock Exchange (hereinafter referred to as 'NSE') and is registered with the Securities and Exchange Board of India (hereinafter referred to as 'SEBI') as a Stock broker under Section 12 of SEBI Act, 1992 with Registration Number INB230782430.
- 1.2 An Inspection of the Books of Accounts, Documents and other records maintained by the broker for the period 2000-01, 2001-02 and April 2002 till date of inspection i.e. 16.9.02 was carried out by SEBI. During the inspection, certain irregularities found to have been committed by the broker were observed.

2.0 APPOINTMENT OF ENQUIRY OFFICER

- 2.1 On completion of inspection, the Report was forwarded to the broker vide letter dated December 31, 2002. After considering its reply dated 15.1.2002, an Enquiry Officer (hereinafter referred to as "EO") was appointed vide order dated December 1, 2003 under Regulation 5(1) of SEBI (Procedure for Holding enquiry by enquiry officer and imposing penalty) Regulations, 2002 (hereinafter referred as the 'said regulations') to enquire into the alleged irregularities committed by the broker which were observed during the inspection.
- 2.2 A Show Cause Notice dated January 12, 2004 was issued to the broker under Regulation 6 (1) of the said regulations. The broker did not reply to the said notice. The EO conducted the enquiry in terms of the said Regulations and the broker was given an opportunity of personal hearing. Shri V Rakesh, representative of the broker appeared for the hearing before the EO and reiterated its reply dated 15.1.03.
- 2.3 After considering the reply and the submissions made at the time of personal hearing, the EO submitted his report dated 18.8.04 recommending suspension of registration of the broker for a period of three months.

3.0 SHOW CAUSE NOTICE AND THE BROKER'S SUBMISSIONS

- 3.1 A copy of the Enquiry Report was sent to the broker along with a show cause notice dated August 24, 2004, in terms of Regulation 13(2) of the said Regulations calling upon it to show cause as to why appropriate penalty including the penalty as recommended by the Enquiry Officer should not be imposed on it. The broker replied vide letter dated September 10, 2004 stating that its director was not in city and would be returning after two weeks and hence requested for time upto September 30, 2004 to submit its reply. Subsequently, the broker submitted its reply vide letter dated October 7, 2004.

4.0 PERSONAL HEARING

- 4.1 An opportunity of personal hearing was granted to the broker on April 27, 2006. Shri.V Rakesh, Authorised Representative of the broker, appeared for the hearing before me and made submissions on behalf of the broker.

5.0 CONSIDERATION OF THE ENQUIRY REPORT

- 5.1 I have carefully considered the findings of Inspection, Enquiry Report and the submissions of the broker and my observations are as under :

(a) Maintenance of Books of Accounts and Records

The EO found that the member had not maintained the Order Book and Margin Deposit Book and hence held the broker guilty of violation of Regulation 17(1) of the SEBI (Stock Brokers & Sub-brokers) Regulations, 1992. I find that the broker did not dispute the charge but stated that since the orders from the clients were received over telephone, it was practically difficult to maintain the order book. I find that maintenance of order book must be strictly complied with and cannot be a matter of convenience of the broker. Maintenance of order book helps in audit trail and receiving and confirming orders over telephone without any record would defeat the purpose. Further, the broker did not furnish any explanation for non-maintenance of margin deposit book. Hence, I presume that the broker has admitted the charge.

b) **Violations in respect of contract notes**

The EO found that the broker had committed the following violations in respect of maintaining contract notes :

- (i) The EO found that the broker had been numbering the contract notes on a daily basis instead of yearly basis. Further, the contract notes had been left blank in between. The EO found that the serial number of the contract notes should be preprinted or system generated on an annual basis and not on daily basis. This requirement has been specified to prevent back dated insertion of serial number in order to prevent tampering or misuse. The broker contended that the company generated contract notes on a daily basis and a new series was generated for each new financial year. The broker further stated that the contract notes were printed on stationery which was page wise and were filed serially as a page
- (ii) The EO found that some contract notes bearing nos. 6851 to 6855 dated 21.11.2001 were not submitted for inspection. The broker stated that the contract notes with the aforementioned serial numbers were not printed as there was a printing error. Since their software does not allow duplicate printing of contract notes, a letter was issued to the client in lieu of the contract note. I note that the broker has not followed the practice of using pre-printed stationery for contract notes which had resulted in missing numbers on account of printing error. Further, the broker has not submitted any documentary evidence to prove that he issued a letter in lieu of the contract note.
- (iii) The EO found that the Trade ID and Time of transaction were not shown in the contract notes issued to certain clients and found it strange that computer error occurred only for selective trades. The contention of the broker was that due to computer error trade ID, transaction ID and time were not printed on the contract notes and the missing contents were informed to the clients.
- (iv) The EO found that the broker had not maintained acknowledgements of clients for contract notes issued and there was no documentary evidence in respect of cost incurred towards postage and courier,. The broker stated that the contracts were sent to the clients by post or courier and hence it was not possible to maintain acknowledgements of contract notes.
- (v) The EO found that the brokerage charged was not shown in the contract notes and it was unclear how there could be a computer error for selective trades. The broker contended that due to computer error, brokerage was not charged to the clients and the brokerage was debited to the client by a debit entry in their account.
- (vi) The EO found that the broker had not submitted the Power of Attorney to the Exchange for authorizing any person to sign contract notes. The general practice was that Mr Meeraaj was signing the contract notes.
- (vii) Therefore, the EO held the broker guilty of violating Clause B(2) of the Code of Conduct specified in Schedule II read with Regulation 7 of SEBI (Stock Brokers and sub-brokers) Regulations, 1992 and SEBI Circular dated 5.8.1996 in respect of the violation relating to contract notes. The broker did not furnish any explanation for this observation.
- (viii) I find that the broker has not refuted the allegations but has given explanations which are vague and lacking in substance as they are not supported by documentary evidence. I find that contract notes are basic documents of utmost importance in the event of arbitration. Hence the broker is required to maintain them in the proper form prescribed. However, the broker has not adopted the prescribed procedure for maintaining the contract notes but has maintained the contract notes according to his convenience which is not in line with the provisions of Bye-laws of Stock Exchanges/ SEBI Regulations.

c) **Non-Collection of margins from clients**

The EO found that the broker had not collected margins from clients where the liabilities had exceeded Rs.1 lakh in a settlement. The EO found that collection of margin is compulsory and hence the broker had violated Circular No.SMDRP/Policy/Cir.33/2000 dated 27.7.2000 read with Cir.6/2001 dated 1.2.2001 which requires that all the clients should deposit a minimum margin of not less than 10% of the net open position of a client. The broker stated that they had taken due diligence of the margins payable by the clients and wherever applicable they had retained the shares as margins and the credit worth of the clients was also considered. However, the broker did not furnish any proof. Further, credit worth of the clients is not a valid ground for not collecting requisite margins. I find that the purpose of collecting margins is in the interest of the broker so that he does not become liable to meet the payment obligations in the event of default.

d) **Non-Segregation of clients' monies**

The EO found that the broker had opened separate accounts for clients' monies. However, clients' funds had been utilized for cash deposits/withdrawals etc. The EO found that 74% of transactions were in the broker's own account and no procedure was followed to calculate profit and loss on these transactions. The EO also found that the broker was taking

physical stock on hand and calculating profit and loss. Hence it was not possible to calculate the misutilisation of clients' funds by the broker.

The EO further found that payments to the clients were not made within 48 hours of payout of the relevant settlements and no authority letter from clients to maintain running account without any obligation to receive payment/delivery within 48 hours was produced by the broker. Hence the EO found the broker guilty of violating circular dated 18.11.93 on segregation of funds. The broker stated that most of the clients were maintaining running account with the broker and payments were made whenever the clients asked for it or the credit balance was maintained with the broker as margins.

I note that the purpose of maintaining separate accounts for clients funds and own funds is to prevent misuse of clients funds by the broker. I further note from the findings of the EO that the quantum of misutilisation of clients' funds could not be calculated. In the absence of any material on record to prove the exact nature and quantum of misutilisation of clients' funds and in the absence of any pending complaints against the broker, I am inclined to give the benefit of doubt to the broker. As regards payments not being made within 48 hours of payout, though the broker claims that the delay was on account of specific request of the clients, there is no documentary evidence in support of its contention.

e) **Non-Segregation of clients' securities**

The EO found that the broker had not transferred securities to clients' DP

accounts from his pool account within 48 hours of declaration of pay-out. The EO found that certain shares of clients were lying in the pool account beyond 15 days without obtaining any written instructions from the concerned clients and hence held the broker guilty of violation of SEBI Circular dated 18.11.93. The broker stated that some of their clients had requested them to retain the shares for immediate selling in the market and for some others the shares were retained as margins. The broker stated that they had obtained written consent from the clients for retaining the shares. However, no such consent letter was produced before the EO. I agree with the findings of the EO that in the absence of documentary proof in support of its contention, the broker's explanation that it had obtained written consent from the clients cannot be accepted.

f) **Non-maintenance of Client Registration Form and Broker-Client Agreement**

The EO found that the broker had not maintained client registration form and broker client agreements for some clients and even when maintained, for some clients it was found to be incomplete. The EO found that none of the client registration forms had any agreement on legally valid paper. Further some non-individual clients had filed registration forms as individual clients. The EO therefore found the broker guilty of violating the Regulations. The broker stated that the defects shown were in the forms opened before 2000-2001 and the accounts have become inoperative now. The details were furnished as per SEBI rules for all the accounts opened after 2001. I find that the Client Registration forms are basic documents necessary for knowing details such as bank account, PAN Number etc which are important and essential to establish the credentials of the clients and also to keep audit trail in case of default. Similarly, entering into agreement with the client before execution of trades is mandatory as per SEBI Regulations.

g) **Unique Client Code**

The EO found that the broker did not allot Unique Client Code. The broker had allotted code to clients based on starting alphabets of broker's name to some clients and numbers to some others. The EO found that Unique Client Code is an essential requirement for trading in an exchange. The broker stated that codes were given to clients according to alphabets etc. before the year 2000 and after 2000 they have been allotting client codes serially from X001 to Z99. I find that the broker has been using its own method to allot Unique Client Code and has not been adhering to the stipulated practice. I note that a prudent stock broker is required to adhere to the provisions stipulated in Rules, Regulations and Bye-laws of Stock Exchanges and not adopt its own practices.

h) **Dealing with unregistered sub-brokers**

The EO found that the broker had traded for certain persons/firms who were registered as clients but were acting as unregistered sub-brokers and hence found the broker guilty of violating Section 12 of SEBI Act. The broker has not given any explanation nor has he refuted the charge. I, therefore, agree with the findings of the EO as dealing with unregistered sub-brokers is in violation of Section 12 of the SEBI Act.

i) **Non-payment of SEBI registration fees**

The EO found that the broker had not paid turnover fees to SEBI and hence it guilty of violating Regulation 10(1) read with Schedule III of the SEBI (Stock Brokers & Sub-brokers) Regulations, 1992. The broker has submitted a copy of statement of fees received from SEBI stating that the broker has paid the fees and there is no outstanding liability. In case there is any shortfall in the payment, separate action may be initiated in accordance with Regulations.

5.2 In the facts and circumstances of the case, I am of the view that a minor penalty of suspension of certificate of registration of the broker for a period of 15 days would be adequate and appropriate.

6.0 ORDER

6.1 Now, therefore, in exercise of powers delegated to me in terms of Section 19 of SEBI Act, 1992 read with Regulation 13(4) of the said Regulations, I hereby suspend the certificate of registration of M/s.Limra Securities Ltd., Member, National Stock Exchange, with Registration Number INB230782430 for a period of 15 days.

6.2 This order shall come into force on the expiry of 21 days from the date of this order.

Place: Mumbai

Date: 16.6.06

T.C. NAIR

WHOLE TIME MEMBER

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