

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

UNDER REGULATION 13(4) SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002 AGAINST M/s INTEGRATED ENTERPRISES (INDIA) LIMITED, DEPOSITORY PARTICIPANT OF NATIONAL SECURITIES DEPOSITORY LIMITED, SEBI REGISTRATION No.IN301313.

WTM/GA/80/ISD/07/06

1.0 BACK GROUND

- 1.1 M/s Integrated Enterprises (India) Limited (hereinafter referred to as the 'IEIL') is a Depository Participant (DP) of National Securities Depository Limited (hereinafter referred to as 'NSDL') and is registered with the Securities and Exchange Board of India (hereinafter referred to as 'SEBI') as a Depository Participant under Section 12 of SEBI Act, 1992 with Registration Number IN301313.
- 1.2 DSQ Software limited (DSQS), is a company listed in Madras Stock Exchange, National Stock Exchange, Bombay Stock Exchange, Delhi Stock Exchange, Ahmedabad Stock Exchange and Calcutta Stock Exchange. Investigation was conducted by SEBI into the alleged manipulation in the scrip of DSQS. Investigations by SEBI, inter alia, revealed irregularities in the allotment of shares by the company, irregularities in the dematerialization of the shares so allotted and irregularities in the sale of the shares so allotted by several brokers and entities associated with the promoters of the company.
- 1.3 The investigation inter alia revealed irregularities in opening the demat account in the name of 'Dinesh Dalmia-Technology Trust' by IEIL as a Depository Participant. Out of the 13 million unlisted shares DSQS floated

in the secondary market, 6 million shares came through the beneficiary account opened with IEIL.

- 1.4 In view of the findings of the investigations, an enquiry was initiated against IEIL for suspected violations of SEBI Act, 1992, Depositories Act, 1996, SEBI (Depositories and Participants) Regulations, 1996 and Bye laws and business rules of NSDL.

2.0 APPOINTMENT OF ENQUIRY OFFICER

- 2.1 An Enquiry Officer was appointed vide SEBI order dated 24.07.2003 under Regulation 5(1) of SEBI (Procedure for Holding enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as 'Enquiry Regulations') to enquire into the alleged opening of the Beneficiary Account in the name of Dinesh Dalmia- Technology Trust for the credit of shares of DSQS.
- 2.2 The Enquiry Officer issued a notice dated 28.11.2000 to IEIL under Regulation 6(1) of the Enquiry Regulations and further granted an opportunity of personal hearing to IEIL. IEIL submitted its reply and appeared for personal hearing. The Enquiry Officer conducted the enquiry in terms of the Enquiry Regulations and IEIL was given a fair and reasonable opportunity to make its submissions. After considering the reply and the submissions made, the Enquiry Officer submitted his report dated January 19, 2005.
- 2.3 The Enquiry Officer made his findings as under;
 - a) IEIL had failed to take into account Clause 13 of the Trust deed which states that the Compensation Committee shall nominate one of the

Trustees to be the Chairman of the Trustees. The Compensation Committee shall also nominate an alternate Chairman from its trustees who shall act in the absence of the Chairman and shall exercise all powers of Chairman. Further, the Enquiry Officer observed that IEIL had accepted the signature of Shri Dinesh Dalmia, one of the Trustees of the aforesaid Trust despite the fact that his name was not authorized by Chairman or alternate Chairman of the Trust as mentioned in clause 13 of the Trust deed. Therefore, there was no document available authorizing Shri Dinesh Dalmia to open the Demat Account in the name of the Trust.

b) With regard to the verification of existence and genuineness of the Trust, the Enquiry Officer observed that mere mentioning of the bank account number is not a sufficient proof of identify because it can not be confirmed whether the bank account was in the name of Dinesh Dalmia Technology Trust or Technology Trust or Dinesh Dalmia etc. In the absence of the requisite document i.e. copy of the bank statement, IEIL had failed to verify the proof of existence of the Trust and therefore, had failed to exercise due diligence while opening the Demat Account in the name of Dinesh Dalmia Technology Trust.

c) As regards the identity of the person who witnessed the agreement between DP and client for opening the account is concerned, the identity of the person was not disclosed. Therefore, there was technical lapse on the part of IEIL as a DP in not obtaining the details of the person who witnessed the DP –client agreement for opening the Demat Account.

2.4 In view of the findings, the Enquiry Officer recommended a minor penalty of 'suspension of Certificate of Registration' of IEIL for a period fifteen days under regulation 13(1) (a) (iv) of the Enquiry Regulations.

3.0 SHOWCAUSE AND REPLY OF IEIL

3.1 After considering the Enquiry Report, a Show Cause Notice dated January 25, 2005 under regulation 13(2) of the Enquiry Regulations was issued to IEIL enclosing therewith a copy of the Enquiry Report. IEIL submitted its reply vide letter dated February 14, 2005, wherein the following submissions were made:

3.2 Vide letter dated February 14, 2005, IEIL submitted as follows :

3.2.1 During the year 2000, the DSQ group was one of the well known groups in Tamil Nadu engaged in activities in various spheres like computer education, biotech, software development, property development etc. Some of the group companies and the family members of the promoter namely Mr. Dinesh Dalmia had opened DP accounts with IEIL. IEIL had no complaints on any issues in the operation of the depository accounts held by Dinesh Dalmia and his family members. In the normal course of business, they had requested us to open the account of the Trust with IEIL. It was informed to IEIL that the Trust has been formed for the purpose of conferring the employees with the benefit of shares under ESOP.

3.2.2 At that point of time, the group was regarded as an extremely vibrant and progressive group and IEIL had no reason to suspect their actions or to doubt the bonafides of Shri. Dinesh Dalmia who was one of the promoters of the DSQS group. IEIL had accordingly provided them, an application for opening a Demat Account and a

standard form of agreement between a depository participant and a client. A copy of the Trust deed constituted by DSQ Software Ltd., and called as The Technology Trust was provided to IEIL. Shri. Dinesh Dalmia was appointed as one of the three Trustees. The said Mr. Dinesh Dalmia had approached IEIL on behalf of the Trust seeking the opening of such Demat Account. Since, Shri. Dinesh Dalmia, was synonymous with DSQ group and IEIL had been furnished with the requisite documents, they had no reason to suspect his bonafides in opening the Trust in the name of Dinesh Dalmia.

3.2.3 Neither in the year 2000, when the DP Account was opened by IEIL nor even as on date, neither SEBI nor NSDL have formulated / issued any guidelines or regulations with regard to opening Demat Accounts in relation to Trusts. IEIL was, therefore, required to use their own judgement in relation to opening such account. According to the prevailing concept, the Demat Account holder would get reflected as a member of the shares held by him in such account, in the books of the company. Keeping this in mind and in view of the fact that Section 153 of the Companies Act prescribes that no notice of any Trust, express, implied or constructive should be entered on the Register of Members, the Demat Account was opened in the name of Mr. Dinesh Dalmia, one of the Trustees of the Trust and in order to identify the capacity in which the account was being opened, the name of the account was specified as "Dinesh Dalmia – Technology Trust".

3.2.4 Clause 13 of the Trust Deed provides for retaining of right to appoint the Trustees of the Trust and to nominate one of those Trustees as the Chairman and another as alternate Chairman by

the Compensation Committee of DSQS. Clause 13 does not anywhere provide that it is only the Chairman who is empowered to act on behalf of the Trust and that unless specific authorization is obtained from him no other Trustee can act. In short, Clause 13 of the Trust Deed did not mandate any authorization to be obtained before opening the Demat Account.

3.2.5 None of the Trustees ever complained that Shri Dinesh Dalmia unauthorizedly opened the Demat Account or transacted business therein. Knowledge of the Trustees about the opening of the account and the transaction in question and absence of any complaint by any of the Trustees establish that Shri Dinesh Dalmia was acting within his authority in opening and operating the Demat Account with IEIL. Trust was formed by DSQS for the benefit of the employees. In the Trust Deed, DSQS is represented by Shri Dinesh Dalmia, its Managing Director. He was also been appointed as one of the first Trustees in the Trust Deed. Therefore, there is no anomaly in opening the Trust accounts in the name of the Trustee as per the general provisions of Companies Act, 1956. There were no circumstances warranting the creation of any suspicion as Dinesh Dalmia representing the author of the Trust approached the DP by representing himself as a Trustee; the account was opened in normal course. Further, there are no guidelines or prescribed procedures with regard to the opening of Demat Account.

3.2.6 The finding of Enquiry Officer that IEIL failed to verify the bank statement is erroneous as IEIL had the details of the bank account Number.155252050 held by the Trust with IndusInd bank, Chennai – 34, at the time of opening the Demat Account. Those details

were furnished in the Demat Account opening form and concerned officer from IEIL had verified the copy of the bank statement issued by IndusInd Bank of the said account. The factum of a subsisting bank account in the name of the Trust is sufficient proof of its existence and IEIL relied on the same to proceed with the opening of the Demat Account.

3.2.7 As IndusInd bank had satisfied themselves with regard to the existence of the Trust and thus permitted the Trust to open such bank account, IEIL could not be faulted in any manner in relying upon such document as proof of existence of Trust. IEIL justified its inability to produce the said bank statement before the Enquiry Officer by stating that the same is not available as there had been shifting of office and the same belonged to a non operative account. IEIL had already communicated with the IndusInd bank requesting a copy of the said account statement and the reply is awaited. And there is no finding against them that there is no account existing in the name of Trust with IndusInd bank.

4.0 **Hearing**

4.1 IEIL was granted an opportunity of personal hearing on February 22, 2006. IEIL appeared for the oral hearing before me through its Chairman Mr. P. Vaidyanathan, Whole Time Director Mr. S. Balasubrahmanyam and CA Mr.Thiagarajan. IEIL made the oral submissions and filed written submissions during the course of personal hearing on February 22, 2006, which are as under:

4.2.1 Either in the Enquiry Report or in the show cause notice referred above, there is no mention of the specific provisions of the SEBI Act, 1992, which is violated. In the absence of reference of the specific violation

either in the Enquiry Report or in the show cause notice, it was submitted that IEIL is not in a position to make their submissions in this regard.

4.2.2 Section 5 of the Depositories Act, 1996 which requires an agreement between the client and the DP for availing the Depository services, casts an obligation on the client. Even assuming there is an obligation under this Section on the Depository Participant, IEIL submitted that they had entered into an agreement with the client in the form specified by the Depository. Besides, there is no finding either in the Enquiry Report or in the Show cause notice to the contrary. Therefore, there is no violation of Section 5 of the Depositories Act, 1996.

4.2.3 There is no finding to the contrary either in the Enquiry Report or in the show cause notice. They had complied with the SEBI Circular No. SMDRP/Policy/Cir-36/2000 dated August 4, 2000. The Circular lists the proofs to be obtained for the Identity and Address of the applicants. The Circular lists the various alternative documents that can be relied upon like Bank Account, Passport, Voter ID, Driving License or PAN Card etc. IEIL relied on the Bank Account details of the beneficial owner.

4.2.4 Bye-law 6.4.1 and 6.4.2 of NSDL Bye laws, reiterate the requirement of DP- client agreement before conducting business as a DP for the client and the same requirement was already met by them. In this regard that there are no findings to the contrary either in the enquiry report or in the show cause notice.

4.2.5 That there is no violation of any of the General Principles listed in Rule 7.1 by IEIL or there is any finding either in the enquiry report or in the show cause notice to that effect. As regards the rules listed in Rule 12.1. for 'Account Opening', the client application is complete in all respects

including the bank account particulars of the client. Hence, there is no violation of any of the rules referred above. Since, NSDL Circulars No.NSDL/P1/2000/1394 dated August 9, 2000 and NSDL/P1/119 dated July 22, 1997 are reinforcement of SEBI Circular dated August 4, 2000 and Rule 12.1.2 of Business Rules, these circulars were complied by IEIL as narrated above.

4.3.6 IEIL had not dematerialized any scrip into the Beneficiary Account. All the credit to this Beneficiary Account was only corporate action. A Depository Participant has no role to play in corporate action and acts merely as an Account keeper. The shares are issued and allotted by a company by a Board Resolution. For allotment of shares under Demat Form, the company makes a formal representation to a Depository, which is NSDL in this case. The Depository collects necessary information with regard to the allotment from the company and from the Registrar. Thereafter, the Depository approves the allotment and gives credit to the individual allottees. In the whole exercise, the Depository Participant has no role to play. This is what has exactly happened in this case.

4.3.7 As IEIL had obtained the DP- Client agreement with requisite details, there is no violation of Regulation 5 and 41 of SEBI (Depositories and Participant) Regulations, 1996 and Bye law Nos. 6.4.1 and 6.4.2 of NSDL Bye laws.

5.0 **Consideration of Issues**

5.1 Before dealing with the issue, it would be appropriate to have a closer scrutiny of documents produced by the DP in the course of enquiry/ investigation. The DP account was opened on the basis of such Documents namely Trust Deed, Application for Account opening and

Agreement with Client. Taking up the Trust Deed first, it is seen that the Deed relates to 'Technology Trust' created by Shri Dinesh Dalmia for the ESOP Scheme. The document available on record is a photocopy of the Trust Deed. It appears that the Trust Deed was made on the 3rd day of October 2000. As per the deed the trustees are:-

1. Shri Dinesh Dalmia
2. Shri Pawan Kumar residing at Chennai
3. Dr. Suryanil Ghosh residing at Calcutta

5.2 The above mentioned persons were to act as Trustees of DSQ Employees Stock Option Trust. Each page of the Trust Deed has been initialed by someone whose identity is neither explicit nor established. Clause 13 of the Trust Deed spells out a mechanism for the appointment of Trustees to be made by the employer. Accordingly the power of appointing the Trustees shall be vested in the Compensation Committee who shall make such appointments in writing. Further Compensation Committee shall nominate one of the Trustees to be a Chairman of the Trustees. Apart from this, the Compensation Committee shall also nominate the Trustee to be an alternate Chairman who shall act in the absence of Chairman and shall exercise all the powers of the Chairman. Clause 20 of the Trust Deed refers to the modalities of the operations of the Scheme. Accordingly, all correspondence in relation to the operation of the Scheme may be conducted by the Chairman and/ or in his absence by the alternative Chairman and in the absence of both by the Trustee authorized in that behalf by the Trustees... The Trustees shall decide which of the Trustees shall operate the bank account on their behalf. The copy of the Trust Deed which is available on record does not contain the signatures of the Trustees and it is not clear whether the Trustees have consented to be so. There is no proof of such verification on record. The Trust Deed is not a

registered Trust Deed. It does not appear to have been made on Stamp Paper. There are no signatures by witnesses, excepting some undecipherable initials. Further there is no accompanying resolution of the Trustees authorizing Shri Dinesh Dalmia to open and operate bank account and demat account for the Trust. A cursory look of the Trust Deed with all the attendant material gaps as detailed supra should normally have alerted even the most unwary of the persons in the DP's office as to the genuineness or otherwise of the Trust Deed. It also appears that no attempt has been made to verify the photocopy with the original of the documents and get the deficiencies supplied, to the satisfaction of the DP, as required by SEBI circular dated 4th August, 2000 addressed to all DPs. As a matter of fact the said circular enjoins that an authorized official of the DP under his signature shall verify the original documents and there is no proof of such compliance. Even assuming that there were no extant guidelines or regulations with regard to opening of demat accounts in relation to Trust, SEBI circular dated 4th August, 2000 should have served as the broad guidelines, as it only stressed what was expected of a prudent person in relation to opening of any new account. The minimum that was required to be verified in the given circumstances was about the genuineness or otherwise of the document as well as the bank account opened by the Trust in IndusInd Bank Ltd, Chennai.

- 5.3 The next significant document which comes up for consideration is the application for opening an account. The application bristles with incomplete details. In addition, it carries account number of the Trust in IndusInd Bank, Chennai and the same is 155252050. On behalf of "Technology Trust", Shri Dinesh Dalmia appears to have signed in the application form. In addition to the parsimony of data in the account opening application, a modicum of basic care does not appear to have been exercised by the DP in relation to ascertaining whether the said Shri

Dinesh Dalmia was competent and authorized to open the account in the absence of a specific resolution of the Trust to that effect and also in terms of Clauses 13 and 20 of the Trust Deed as gathered. In my view, in the absence of enabling resolution coupled with equally material absence of the recommendation of the Compensation Committee, the acceptance of the signature of Shri Dinesh Dalmia in the account opening form on behalf of the holder signifies signal failure of minimum real time check on the part of DP before acting on the application for account opening. Similarly I find that the DP has not carried out such verification in relation to bank account mentioned in the application and the facile plea of DP that the papers relating to verification has been lost during shifting of the office appears to be just an afterthought. Verification independently made by SEBI with CBI, Delhi, who are also investigating into the case of DSQ Software Ltd clearly indicates that the said account 155252050 belonged to a customer by the name of A. Manoharlal. This is evidenced by the communication addressed by IndusInd Bank to CBI, Delhi on 20th February, 2006. The communication further goes on to say that no savings or current account was opened and that the account was never operative. The above clarification provided by IndusInd Bank to CBI, Delhi establishes beyond doubt that the account No. 155252050 did not really belong to the Technology Trust as declared in the application for account opening. As a matter of fact this communication has been shown to the DP and their reply has been equivocal to parry the inconvenient question. The short point to be considered is how the DP could have verified the bank account when it did not exist and obviously the same nails their explanation to the counter.

- 5.4 The third document which is equally important for consideration, is the agreement for the DP and the client as per the extant byelaws of NSDL, under byelaw no.6.4.1. It states that no participant shall conduct

business as participant with its clients unless it has entered into agreement with its clients. Accordingly the agreement between the DP and the client becomes another important document. In the instant case, the agreement was entered into on 9th October, 2000 and the agreement has been witnessed to by someone whose initials are not identifiable. Also the question whether Shri Dinesh Dalmia was competent and authorized to enter into agreement with the DP remains, in as much as there is no resolution to that effect by the Trustees of the Trust authorizing Shri Dinesh Dalmia to enter into such an agreement and further in as much as Clause 13 read with Clause 20 of the Trust Deed does not automatically empower Shri Dinesh Dalmia to enter into such an agreement with the DP.

- 5.5 The above observations based upon some of the documents relevant to opening of a demat account by the DP make it evident that the DP did not exercise basic care and prudence which is expected of a DP. Even assuming that there were no extant guidelines or prescribed procedures with regard to opening of demat account of a Trust, it cannot be gainsaid that there were guidelines on the subject at the relevant point of time. As already stated, SEBI circular dated 4th August 2000 stresses that it is extremely important that all documents are verified with the originals and photographs and signatures duly authenticated before accounts are opened. Further it is added that the same are critical steps for the safety, integrity and efficient functioning of the depository system and that any failure in that regard could invite appropriate regulatory action. Verification with original would include all the scrutiny of the original as complete document evidencing the existence of a valid Trust, going beyond a physical matching. The said circular clearly imposes a duty of verification on the DP, in the same manner as what is expected of a normal prudent person acting in such circumstances.

5.6 The observation of the DP that Shri Dinesh Dalmia was a well known person in business and that therefore there could be no circumstances warranting any suspicion regarding competence of Shri Dinesh Dalmia as a Trustee cannot cut much ice, since the basic precaution to be observed in opening new DP account cannot be dispensed with on the specious plea that the author of the Trust was well known in business world. The basic guidelines are applicable in all circumstances irrespective of the standing of the person concerned and any relaxation in the observance of basic elementary precaution is fraught with dire mischief as happened in this case subsequent to the opening of the DP account, when the account turned out to be the fountainhead of unmitigated market mischief. Similarly there has been abject failure in the verification of the bank account of the Trust as borne out by the documentary evidence. Such verifications which are not idle formality are prescribed to satisfy that the documents do evidence the existence of these arrangements or accounts which they represent and are meant to be a check against any form of misrepresentation to cheat.

5.7 In short such verifications have not been carried out by the DP, while accepting the crucial documents without minimum scrutiny as mandated. The position of Shri Dinesh Dalmia is no answer to such glaring lapse. Further, the acceptance of Shri Dinesh Dalmia as an authorized person of the Trust without the necessary resolution to that effect and without insisting on the requirements of Clauses 13 and 20 of the Trust Deed is again proof of the fact that minimum verification was given a short shrift on the strength of the standing of Shri Dinesh Dalmia. The guidelines relating to verification cannot be sacrificed on the altar of the seeming importance of the person, since such an act can be the thin end of the

wedge, paving the way for several egregious developments as happened in the instant case. As a matter of fact the orders passed by SEBI in September/ October 2004 against DSQ Software Ltd, their promoters, directors, associated entities etc. clearly brings out that Shri Pawan Kumar one of the Trustees based at Chennai was not aware of the Trustees at all though his name was mentioned as one of the Trustees of Dinesh Dalmia Technology Trust and Softec Corporation. Similarly, Dr. Suryanil Ghosh who was also mentioned as one of the Trustees of the Trust was not available at the given address as the address itself was found to be incorrect. In that view of the matter though such findings might have transpired in the orders passed by SEBI in September/ October 2004, the fact remains that the Trust was to all intents and purposes a front of Dinesh Dalmia for his questionable designs to get unfair advantage to himself and to his associates by exploiting the markets and cheating the investors.

- 5.8 The findings in those orders of SEBI indicate that 1,00,00,000 shares were fraudulently allotted by DSQ software, 60,00,000 shares of DD Technology Trust and 40,00,000 shares to Dr. Suryanil Ghosh Trustee, Softec Corporation. These shares were allotted in electronic form and under the same ISIN under the same existing shares were being traded. These shares were issued without following the procedure under Company Law. These shares were sold in the market by entities associated, with DSQ group like DSQ Holdings, Powerflow Holding and Hulda Properties without being listed on any stock exchanges. These shares were delivered in the market knowingly that the shares did not have listing permission. Since the shares were issued under the same ISIN it was considered as good delivery by investors because distinctive numbers of the shares could not be traced in the dematerialized form. Taking advantage of the provisions

that the company could allot further shares under the same ISIN the company allotted the above shares to the aforesaid trusts in the demat accounts. These shares were then brought into the market by either delivering them directly to pool account of brokers against the sales by group entities or indirectly by first transferring the shares to account of group entities and then selling them into the market. Though the DP might claim that they could not be expected to know in advance whether the account would be misused, or not, the point that is being stressed at this juncture and for the purpose of this order is that, had the DP followed the basic precaution in relation to the opening of new DP accounts as is brought out by SEBI circular dated 4th August, 2000 duly reinforced by NSDL in their circular dated 9th August, 2000 communicated to all DPs, the major market misconduct as mentioned above could have been averted. Though nobody can be judged by hindsight, it would be equally important to reckon with that a posteriori development which has a causal relationship with real time failure does have a bearing on it, besides setting it on the canvas of subsequent developments.

- 5.9 By virtue of the same, IEIL is guilty of violating SEBI Circular No.SMDRP/Policy/Cir-36/2000 dated August 4, 2000 and NSDL Circulars Nos.NSDL/P1/2000/505 dated April 18, 2000, NSDL/P1/2000/1394 dated August 9, 2000 and NSDL/P1/119 dated July 22, 1997 and thereby in turn violating NSDL Business Rules 7.1.1 and 7.1.2 and Regulation 20 (2) (b) of SEBI (Depositories and Participant) Regulations, 1996.

6.0 ORDER

- 6.1 After careful consideration of the submissions made by the DP and the facts available on record, in exercise of powers conferred under upon me in terms of Section 19 of SEBI Act, 1992 read with Regulation 13(4) of the Enquiry Regulations, I hereby direct the certificate of registration of M/s Integrated Enterprises (India) Limited, Depository Participant of NSDL having SEBI Registration No.IN301313 be suspended for a period of 15 days except for acting on the instructions of existing beneficial owners, so that the interests of existing Beneficiary Owners remain unaffected.
- 6.2 This order shall come into effect three weeks from the date of the passing of the order.

Place: Mumbai
Date:10-08-2006

G. Anantharaman
Whole Time Member
Securities and Exchange Board of India