

SECURITIES AND EXCHANGE BOARD OF INDIA, MUMBAI

Coram: V.K. CHOPRA, WHOLE TIME MEMBER

In the matter of

VINOD KUMAR & Co., MEMBER,

U.P. STOCK EXCHANGE ASSOCIATION LTD.

SEBI REGISTRATION NO. INB 100694710

WTM/VKC/MIRSD/4/09/06

Date of hearing : 26-07-2006

Appearances

For Noticee : Party did not appear
For SEBI : Mr. P. K. Kuriachen, General Manager

ORDER

**(Under Regulation 13(4) of SEBI (Procedure of Holding Enquiry by
Enquiry Officer and Imposing Penalty) Regulations, 2002)**

1.1 Vinod Kumar & Co. (hereinafter referred to as "broker") is a proprietary concern and registered with Securities and Exchange Board of India (hereinafter referred as SEBI) as a broker of Uttar Pradesh Stock Exchange Association Ltd. bearing SEBI Registration No. (INB 100694710). The broker is also a sub-broker of BSE affiliated through the UPSE Securities Ltd. (a subsidiary of UPSE) with SEBI Regn. No. INS 010789415.

1.2 Securities and Exchange Board of India (hereinafter referred to as SEBI) carried out an inspection under Regulation 19 (1) of SEBI (Stock Brokers and Sub Brokers) Regulations, 1992 (hereinafter referred as the Broker Regulations). The inspection was carried out for the period of April 01, 2001 to March 31, 2003 by Nripendra & Co., Chartered Accountants. During the inspection, several irregularities / violations were found to have been committed by the broker.

2. Enquiry Proceedings

2.1 Upon considering the findings of inspection, an Enquiry Officer was appointed under Regulation 5 of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as the Enquiry Regulations) vide order dated March 31, 2004.

2.3 A Show Cause Notice (hereinafter referred as SCN) dated April 29, 2004 was issued to the broker under Regulation 6 (1) of the Enquiry Regulations. The broker submitted its reply vide letters dated May 15, 2004. The broker had also availed the opportunity of personal hearing on August 12, 2004. After considering the reply of the broker, the Enquiry Officer proceeded with the enquiry and submitted her report dated October 07, 2004 recommending suspension of certificate of registration of the broker for a period of six months.

2.3 A copy of the Enquiry Report was issued to the broker along with a SCN dated October 18, 2004, in terms of Regulation 13(2) of the Enquiry 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 had replied to the said SCN vide its letter dated October 28, 2004.

2.4 The broker was given an opportunity of personal hearing before me on July 26, 2006. But on the designated date no one was present on behalf of the broker. However the broker filed written submissions.

3. Consideration of Issues

3.1 I have carefully considered the Inspection Report, Enquiry Report, SCN to the broker, its replies dated October 28, 2004 and written submissions dated July 17, 2006 and find as follows:

(a) Dealing as an Unregistered Entity

Regarding the findings that the broker has been dealing as an unregistered sub-broker at NSE, it was stated by the broker that it was trading with Tag Finvest which is a trading concern only. The Enquiry Officer further found that the broker can deal on the platform of NSE only through a member of NSE but in present circumstances the broker is operating as a sub-broker of some NSE broker and present entity is only for the purpose of routing its transactions. The broker has not

given any satisfactory reply to this charge at any stage of the enquiry proceedings. The only defense the broker had taken is that the inspection authority was empowered to inspect about the trades at UP Stock Exchange only. By taking this defense broker can not violate SEBI Circular SMD/Policy/Cir-3/98 dated January 16, 1998 and section 12 of SEBI Act, 1992.

(b) Non maintenance of Books of Accounts etc.

With regard to the findings that the broker had not maintained the proper books of account, the inspecting authority pointed out that the trades done for clients were first done in its own proprietary account and later on these were found to be transferred to the client's account. The reply of the broker on this point is not clear, though the broker had submitted before the inspecting authority that all the business has been done on 'Own Account'. Enquiry Officer found that these acts reflect lack of transparency on the part of broker. I agree with the findings of the Enquiry Officer that the broker has to maintain high standards of integrity and fairness in all conducts of its business. By doing the above broker has not complied with the Code of Conduct prescribed by SEBI under Schedule II of Broker Regulations.

(c) The broker was not maintaining Order Book

Regarding the findings that the broker has not maintained the order book, it was admitted by the broker therefore it's a clear violation of SEBI Circular No. SMD/Policy/IECG/1-97 dated February 11, 1997 which stipulates that the broker should maintain the record of time when the client has placed the order. Therefore, I agree with the views of the Enquiry Officer that the broker is not maintaining the order book and has violated the procedure laid down by SEBI. However this breach may not warrant substantive penalty.

(d) Contract Notes

With regard to the findings that the broker was not issuing contract notes in respect of any of the transactions entered and executed for and on behalf of the clients in reply the broker replied that it had not dealt with any client as a member of UPSE and it was issuing only the confirmation notes to all of its client being a sub-broker. In light of these submissions, I am inclined to take a lenient view.

(e) Margin Deposit Book

With regard to the findings that the broker had not maintained the margin deposit book, the broker submitted that the margins with UPSE has been properly maintained and recorded in the books of accounts. This explanation of the broker is incomplete as no proof has been presented or submitted either before inspecting authority or before Enquiry Officer.

(f) Client Database

With regard to the findings that the broker has not maintained proper client database, the broker submitted that it has not dealt with these client as a member of UPSE but as a sub-broker and therefore these obligations are not applicable to it. The contention of the broker is not correct, as on interpretation of the circular No. SMD/Policy/IECG/1-97 dated February 11, 1997 and SMD/Policy/Cir 5-97 dated April 11, 1997, the obligation should be applicable to the sub-brokers as well and if not, the whole purpose of Know Your Client will be defeated. The SEBI Circular SMD/Policy/Circular/ 11 -97 dated May 21, 1997 is clear on this point. The said circulars stipulate that members should maintain a database of their clients like ID Proof, Pan No., letter from the bankers certifying the account number in the format suggested by SEBI i.e. Client Registration Form and Broker Client Agreement. At the time of personal hearing, broker had presented xerox copies of some Individual Client Registration Application Forms to the Enquiry Officer for perusal. It is observed from the same that the said forms are not dated, they are not in prescribed format like account number, PAN number, introducer name, identity proof etc are not there. In these circumstances I find that the broker has not maintained proper client registration as required by the above said circulars. Hence I agree with the findings of the Enquiry Officer and hold broker guilty on this count.

(g) Payment/ delivery to clients

With regard to the findings that the broker had not made the payment/ delivery to the clients within the prescribed period of payout i.e. 48 hours. The inspection team has also given some illustrative case where the pay-out was not made in time. In addition to this the inspection authority found that there was no general authority from the clients to maintain/operate the account on 'running basis'. In reply to this, broker made some general submissions and stated that it has no dispute regarding any matter with its clients till date and also that no matter has been registered with UPSE securities or SEBI from any of its client. The broker had also submitted that the clients in respect of which registration forms were brought have given their consent to retain payments/ deliveries for further trades. However, no proof of the same has been submitted with these submissions. This explanation given by the broker is very vague in nature. The Enquiry Officer has confirmed the fact that there is no complaint from clients. In view of this and considering that number of such clients is few, I am inclined to take a lenient view.

(h) Funds and Resources

With regard to the finding that the broker was not maintaining separate bank accounts for its own funds and the clients fund and there was no clear segregation of client's funds and the broker's money. In addition to this it was also observed by the inspecting authority that broker has transferred/adjusted balance lying in one client's account to another client's account without having any such authority from either of the clients. The reply of broker on this charge is not clear. It is compulsory for all the brokers to keep the client's money in separate account at a bank, with the name "clients" appearing in the name of the account. This provision has been stipulated to prevent misuse of client's funds by the broker. Though the broker has submitted that there is no complaint from clients, by this broker can not override a compulsory rule as it should had segregated own funds from clients funds to prevent probable misuse of client's funds as this measure is to ensure the market integrity. However, since there is no finding of misuse of client funds, I am inclined to take a lenient view.

(i) Unique Client Code

With regard to the finding that the broker has failed to maintain and use Unique Client Codes, the reply of broker is not clear. By not maintaining Unique Client Code the broker violated SEBI Circular SMD/Policy/Cir-39/2001 dated July 18, 2001. I have, therefore, no reasons to disagree with the Enquiry Officer.

(j) Model Code of Conduct for Prevention of Insider Trading

With regard to findings that the broker has failed to comply with the provisions of Regulations 12 (2) and 12 (3) of SEBI (Prohibition of Insider Trading) Regulations, 1992 (hereinafter referred to as Insider Regulations) which deals with the introduction of model code of conduct for prevention of insider trading for entities specified in Schedule-II of the said Regulations, the broker has to adopt appropriate mechanisms and procedures to enforce the code as specified under the aforesaid Regulations, which it failed. Hence, I agree with the findings of the Enquiry Officer and find the broker guilty on this count.

3.2 I have noted the submissions of the broker that its trading terminal has been deactivated by UPSE on surrender of its certificate of registration on May 12, 2004. However, this can neither be a defense for escaping the penalty nor it precludes SEBI from passing this order on merits. It is open for the broker to get the certificate of registration forwarded through UPSE to SEBI for cancellation in accordance with the Regulations.

3.3 Having regard to the gravity of charges established and in the facts and the circumstances of the case, I am of the view that a penalty of suspension of certificate of registration for fifteen days would be adequate.

4. Order

4.1 Now, therefore, in exercise of the powers conferred upon me in terms of Section 19 of the SEBI Act, 1992 read with Regulation 13(4) of the SEBI (Procedure of Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations 2002, I hereby impose a minor penalty of suspension of certificate of registration for a period of fifteen days on Vinod Kumar & Co., member, UPSE Ltd., bearing SEBI Registration No. INB 100694710.

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

Mumbai

Date: 06.09.2006

V.K. Chopra

Whole Time Member

Securities and Exchange Board of India