

SECURITIES AND EXCHANGE BOARD OF INDIA, MUMBAI

Coram: V.K. CHOPRA, WHOLE TIME MEMBER

In the matter of

M/s. KANUDIA CAPITAL AND MANAGEMENT SERVICES (P) LTD., MEMBER, U.P. STOCK EXCHANGE ASSOCIATION LTD.

SEBI REGISTRATION NO. INB 100933132

WTM/VKC/MIRSD/2/08/06

Date of hearing : 25-07-2006

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** Kanudia Capital & Management Service (P) Ltd. (hereinafter referred to as "Kanudia" or "broker") is a corporate entity and is a broker of Uttar Pradesh Stock Exchange Association Ltd. bearing SEBI Registration No. (INB 10093312).
- 1.2** Securities and Exchange Board of India (hereinafter referred as SEBI) carried out an inspection of the books of accounts of the broker 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 June 30, 2003 by Ramesh C. Agrawal & Co., Chartered Accountants. The inspection report was submitted on August 29, 2003. 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.
- 2.2** 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 August 12, 2004 and November 09, 2004. The broker had not availed the opportunity of personal hearing. After considering the reply of the broker, the Enquiry Officer proceeded with the enquiry and submitted her report dated December 1, 2004 recommending a minor penalty of suspension of certificate of registration of the broker for a period of 30 days.
- 2.3** A copy of the Enquiry Report was issued to the broker along with a SCN dated December 14, 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 not replied to the said SCN.
- 2.4** The broker was given an opportunity of personal hearing before me on July 25, 2006. None appeared on behalf of the broker.

3. Consideration of Issues

- 3.1** I have carefully considered the Inspection Report, Enquiry Report, SCN to the broker and its replies dated August 12, 2004 and November 9, 2004 and find as follows:

(a) Irregularities in maintenance of Order Book

Regarding the findings that the broker has not maintained the order book, it was stated by the broker that the orders were simultaneously entered as and when received through the telephone. The order numbers as claimed by the broker was generated by the trading software and is printed along with the time on the contract note issued to the client. The explanation given is not sustainable as the broker had failed to submit any proof of the same.

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 in its 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. This has to be maintained by the broker in

the form of order book. Therefore, it is necessary for the broker to comply with the requirement of maintaining registers as per the SEBI Regulations/ Circulars.

(b) Irregularities in maintaining Document Register

With regard to the findings that the broker had not maintained the document register, the broker submitted that the said register is being maintained by it, but as the scrips traded for the clients by the broker were in Demat form hence the register remained blank. I find that document register is a primary record which contains the particulars of securities received or delivered by the application of Regulation 17 (1) (g) of Broker Regulations, 1992. I agree with the findings of the Enquiry Officer that the broker cannot do away with the necessary requirement of the document register on the ground that it does not have scrips in physical form. Moreover, the broker has not produced any printed copy of the electronic record.

(c) The broker was found to be not maintaining the Margin Deposit Book

With regard to the findings that the broker had not maintained the Margin Deposit Book the broker replied that margins were kept in separate accounts of the client and this deposit book is maintained in the computer and no manual register is maintained for the purpose.

I do not find any proof of the said separate account. The broker had neither produced the computer generated record book to the inspecting authority nor had it submitted a copy to the Enquiry Officer hence this is a violation of Regulation 17 (1) (k) of Broker Regulations.

(d) Contract Note

With regard to the findings that the broker was using computer generated contract note which doesn't facilitate a serial number, the broker replied that the order number has been mentioned on the face of the contract note. But the reply was not satisfactory as the contract note given to SEBI during inspection doesn't show the number. In another reply the broker has submitted that it has amended the software and now the contract notes are serially numbered by the computer. This submission shows that the broker is taking corrective measures. In light of these corrective measures, I agree with the findings of the enquiry officer that it is not a serious violation to call for any penal action.

(e) Collection of Margin from the Clients

With regard to the findings that the broker had not collected the margin money from his clients either in the form of cash or bank guarantees or in the form of FDRs, the broker replied that it had got authorization from its clients that money and shares due to him be transferred to there margin account. However the broker has not produced such authorization.

Further in terms of SEBI Circular No. SMD/SED/Cir/93/23321 dated November 18, 1993 and SEBI Circular No. SMDRP/Policy/Cir-06/2001 dated February 01, 2001 the broker being a registered intermediary is expected to understand the importance of the margin deposit as a risk containment measure. The broker has to ensure himself that it should collect the stipulated margin money from all the clients in the form of cash, bank guarantees, FDRs or other approved securities which shall not be less than 10 % of net open position of a client at any time. Since there was no findings of default to the exchange by the broker by not collecting margins from the clients, I am inclined to take a lenient view on this issue.

(f) 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 alleged that the broker had been obtaining general authority from their clients to keep funds and delivery of scrips for the clients' obligation in the subsequent settlements. In reply to this, broker submitted that sometimes clients instead of giving fresh margin, gives a written authority that funds/shares due to him be kept as their margin. The enquiry officer in its report had found that there is no complaint from the investors against the broker and as the purpose of this policy is to protect the interest of investors, hence the violation is not serious enough to attract any statutory action. I agree with the findings of Enquiry Officer.

(g) Carry Forward transactions

With regard to the findings that the broker has carried out certain transactions which are suspected to be unauthorized carry forward transactions, the Enquiry Officer after considering the inspection report, trade log and the submissions of the broker found that the data available is not sufficient to prove the charges as there is no mention who is the counter party client in the trade and only the name of the counter party broker is displayed. The inspecting authority has not given any other evidence except the observations that the transactions were reversed on the subsequent day with the same quantity and with the same counterparty. After a careful consideration of the material on record I am inclined to give benefit of doubt in favour of the broker.

(h) Funds and Resources

It was alleged that the broker was operating from same account for both the client's fund and broker's fund in violation of the SEBI Circular No. SMD/SED/Cir/93/23321, based on the fact that the client's account in HDFC bank (A/c no. 127034000600) is not used. The broker submitted that the client's money was utilized for client's purpose and there is no case filed against it by any client in grievance cell of U.P. Stock Exchange association. This submission is unacceptable as 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. Considering the submissions of the broker that there is no complaint from clients and that there is no finding of misuse of client funds, I am inclined to take a lenient view.

(i) Submission of Audited report

With regard to the findings that the broker had not submitted the copy of the audited financial statement for the year 2000-2001 the broker submitted that the report has been filed with the U.P. Stock Exchange. Considering this a lenient view is taken.

3.2 From the aforesaid, I find that the violations are technical and procedural irregularities and no substantial punishment is called for. In the facts and circumstances of the case, I am of the view that a penalty of censure would be adequate and act as a deterrent on the broker.

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 penalty of censure on M/s Kanudia Capital and Management Services (P) Ltd., member, UPSE Ltd., bearing SEBI Registration No. INB100933132.

4.2 This order shall come into force with immediate effect.

Mumbai

Date: 30.08.2006

V.K. Chopra

Whole Time Member

Securities and Exchange Board of India