

SECURITIES AND EXCHANGE BOARD OF INDIA

CORAM: V.K.CHOPRA, WHOLE TIME MEMBER

IN THE MATTER OF

M/s. SAKSHI STOCKS AND SHARES PVT. LTD.

MEMBER, UTTAR PRADESH STOCK EXCHANGE

SEBI REGISTRATION NO. INB 100858538

WTM/VKC/MIRSD/6/09/06

DATE OF HEARING: 25.07.2006

APPEARANCE :

FOR NOTICEE : Mr. Deepak Gupta, Director

FOR SEBI : Shri P. K. Kuriachen, General Manager

ORDER

(UNDER REGULATION 13(4) OF SEBI (PROCEDURE FOR HOLDING ENQUIRY BY ENQUIRY OFFICER AND IMPOSING PENALTY) REGULATIONS, 2002)

1.1 Sakshi Stocks and Shares Pvt. Ltd. (hereinafter referred to as "the broker") is a member of the Uttar Pradesh Stock Exchange ("UPSE") registered with SEBI as a stock broker under section 12 of SEBI Act, 1992 with SEBI Registration No. INB100858538.

1.2 Inspection of the books of accounts, documents and other records maintained by the broker for the period from April, 2001 to March, 2003 was carried out by V. Khanna & Company, Chartered Accountants, on behalf of SEBI. Certain irregularities/contraventions of SEBI Regulations were observed during the said inspection. A copy of the Inspection Report was sent to the broker vide letter dated 22.09.2003 and his comments thereto were received vide reply dated 23.12.2003.

2.0 Enquiry Proceedings

2.1 An Enquiry Officer (EO) was appointed vide SEBI Order dated 22.03.2004 under Regulation 5 of SEBI (Procedure for holding enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as 'said regulations') to enquire into the alleged contraventions observed during the inspection of books of accounts of the broker.

2.2 A show cause notice dated 28.04.2004 in terms of Regulation 6(1) of the said Regulations was issued to the broker. The broker vide its letter dated 30.08.2004 and 15.09.2004 submitted its written reply.

2.3 As per the request of the broker, an opportunity of personal hearing was given to the broker by the EO on 27.10.2004 which was attended by the broker, who made oral submissions.

2.4 The EO after conducting the enquiry in terms of the said regulations submitted his report on 02.12.2004 and recommended a penalty of suspension of registration of the broker for a period of four 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 15.12.04, in terms of Regulation 13(2) of the said regulations, advising the broker to show cause as to why an appropriate penalty including penalty as recommended by the EO should not be imposed. The broker replied vide letter dated 04.01.2005 and also submitted that he should be exonerated in view of the latest citation SEBI vs Cabot International Corporation, (2004) 51 SCL 307 (BOM).

3.2 An opportunity of personal hearing before me was given to the broker on 25.07.2006. Mr. Deepak Gupta, Director of the broker appeared and made his submissions.

4.0 Consideration of issues

4.1 I have carefully examined the facts and circumstances of the case, the inspection report, the Enquiry Report and the submissions of the broker thereto and my observations are as follows:

4.1.1 Non-maintenance of Document register:

With regard to the charge that the broker had not maintained the Document register, the EO found him guilty of violating Regulation 17(1)(g) of SEBI (Stock broker and Sub broker) Regulations, 1992 since the broker had not furnished relevant documents to prove his contention that he had maintained script wise and client wise stock register. The broker had replied that Regulation 17(1)(g) provides that in case of dematerialized securities, the Document register should contain the statement of account of the record relating to the receipts and delivery of securities provided by Depository Participants and since the broker had dealt with dematerialized securities during the inspection period, the records had been maintained as per the above regulation and the broker's records were destroyed in fire on 15.04.2004 and a copy of the statement provided by Depository Participants was given as proof. I am of the opinion that the document register is the primary record for shares and securities held by the broker on behalf of his client and for himself and also it is a statutory requirement. The broker is expected to maintain Document Register to keep a record of shares and securities held by it. The statement of Depository Participants does not absolve the broker from maintaining the Document Register. However, I am inclined to take a lenient view since the records of the broker had stated to have been destroyed in the fire accident and he had produced the copies of statements provided by the Depository participants.

4.1.2 Non-routing of transactions through client Bank account:

The EO found that the broker had not routed the transactions of the client through the client Bank account and found him guilty of violating SEBI Circular No.SMD/SED/CIR/093/23321 dated 18.11.1993 since the broker had admitted the same. The broker had replied that it had never misused the clients fund in any manner and no specific charge had been made regarding the misuse of clients money by the Inspecting Authority and hence, the charge could not sustain. The broker further submitted that SEBI circular allows payment in cash upto Rs.20,000/- and the same is allowed under Income Tax Act, 1961. The perusal of the Inspection Report shows there had been 10 instances where the broker had accepted cash from the client. Nowhere in the SEBI Circular No. SEBI/MRD/SE/Cir- 33/2003/27/08 dated 27.08.2003 that payment in cash upto Rs.20,000/- is allowed and it had mentioned only in exceptional circumstances cash payment is allowed to the extent not in violation of the Income Tax requirement as may be in force from time to time. The broker had not shown evidence in proof that there was exceptional circumstances to receive cash from the said clients mentioned in the Inspection Report. It is clear that the broker had violated the aforesaid provision and had admitted the same. Moreover, the broker had not provided any proof there was segregation of the accounts of the client and the broker. However, since there is no findings of misuse of client funds, I am inclined to take a lenient view in this regard.

4.1.3 Contract notes did not bear pre-printed serial Nos. and delay in delivery of Contract notes:

The EO found that the broker had not issued the Contract notes with pre-printed Serial Nos. and there was delay in delivery of Contract notes and found him guilty of violating SEBI Circular No. SMD/MDP/CIR/043/96 dated 05.08.1996 since the broker had failed to support his contention with relevant document that he had issued the Contract notes as required by SEBI and delivered it in time and the broker had failed to maintain the registers. The broker had replied that the contract notes contained pre-printed Serial Nos. and documentary evidence regarding the same was submitted and the SEBI Circular dated 05.08.1996 does not mention to maintain any register and hence, he had not violated any provisions. I perused the Contract notes filed by the broker in support of his claim that it was in order. I found that there were pre-printed Serial Nos. but the order time, order number, trade time were not printed in the contract notes which is also violation of SEBI Circulars. But since there is no charge framed against the broker in this regard, I am inclined to take a lenient view. Further, the broker had not provided any proof regarding the delivery of Contract notes within the specified time of 24 hours and I hold him guilty of violating the aforesaid provisions.

4.1.4 Acted as unregistered Sub-Broker:

The EO found the broker guilty of violating the provisions of SEBI Circular No.SMD/Policy/CIR-3/98 dated 16.01.1998 since the broker had acted as unregistered Sub-broker of JV Stock Broking Pvt. Ltd and terms of Rule 3 of SEBI (Stock Brokers and Sub Brokers) Rules, 1992 read with Sec 12 of SEBI Act states that no stock broker or sub-broker shall buy, sell and deal in securities unless he holds a certificate granted by the Board under the regulations. The broker replied that SEBI Circular dated 16.01.1998 states that member of Stock Exchanges executing transactions through the member of other Stock Exchanges are to be treated as Sub-brokers. Since, the broker and the said JVST Stock Broking Pvt. Ltd are members of the same Exchange, i.e. UPSE, the said circular was not applicable. The broker further submitted that JV Stock Broking Pvt. Ltd was Sub-broker of BSE/NSE and hence the said circular would be applied if JVST Stock Broking had been a member of NSE/BSE and not a Sub-broker of the said Exchanges. The broker further submitted that Circular dated 17.01.2004 states in para 3.3 that a Sub-broker of an Exchange can deal with only one broker of another Exchange on behalf of client after obtaining necessary registration as Sub-broker and since the said circular deals with the situation where a broker of the Exchange deals with only a Sub-broker of other Exchange and not the broker of the other Exchange and also the above circular dated 17.01.2004 overrides earlier circular of 1998 and hence, registration of Sub-broker was necessary to be obtained from 17.01.2004 and hence, he had not violated any provisions. I am of the view that the broker himself admits that he had acted as sub-broker of JV Stock Broking Pvt. Ltd knowing well that he is not registered as sub-broker of the concerned broker and he cannot circumvent the provisions on the ground of technicalities. When a member of the Stock Exchange executes trades for his clients through the other member of the same Exchange or other Exchange, he would be

acting as a Sub-broker. Moreover, the circular No. SEBI/MIRSD/Cir-06/2004 dated 13.01.2004 referred by the broker clearly states in para 3.1 that " *A Stock Broker/Sub-broker of an Exchange cannot deal with Brokers/Sub-brokers of the same Exchange either for proprietary trading or for trading on behalf of clients, except with the prior permission of the Exchange*". Since the broker had transactions as unregistered sub-broker with JV Stock Broking Pvt. Ltd., I agree with the view of the EO and hold the broker guilty of violating the aforesaid provisions.

4.1.5 Non collection of margins from the clients and delay in payment to the clients:

The EO found the broker guilty of violating the provisions of SEBI Circular No.SMD/Policy/CIR-12 dated 17.05.2002 and Circular dated 01.02.2001 since the broker did not collect the margin from the clients and delayed in payments to the clients and found that the reply of the broker that the clients deposited the cheques towards the margins daily and took back the same at the end of the day by squaring up the transactions were not proper as the margins are to be realized by the broker and also the broker failed to deliver the securities to the clients. The broker replied that he had proved sufficiently through bills that the transactions of the client had been squared up on the same day and so there was no question of any net open position regarding persons mentioned in Inspection Report and they had enclosed Letter of Authority for compliance of margin requirement. The broker further submitted that it had not defaulted in deposit of margin to the Exchange and the same was informed by UPSE. The broker further submitted that the clients had given the mandate to withhold and detain the delivery/payment unless instructed by them and hence, the broker had not violated any provisions. I am of the view that the collection of margin is a risk management measure and 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 by the client and he is expected to collect margins in the form of securities, money, FDRs, etc. Moreover, the broker had not delivered the securities to the clients in time. The letters of authority produced by the broker in support of his contention is not dated which raises doubt about the genuineness of those letters. However, since there had been no complaint against the broker and no instances of defaulting to the Exchange, I am inclined to take a lenient view in this regard.

4.1.6 Non-maintenance of Unique Client Code and discrepancies in KYC forms:

The EO found the broker guilty of violating the provisions of SEBI Circular Nos. SMDRP/Policy/CIR-39/2001 dated 18.07.2001 and SMD/Policy/IECG/1-97 dated 11.02.1997 since it failed to maintain Unique Client Code and for discrepancies in KYC forms since maintenance of both is a mandatory requirement. The broker replied that SEBI had introduced Unique Client Code from 18.07.2001/11.02.1997, but the said circular was applicable for clients having order value of Rs.1 lakhs and not for all clients as is evident by UPSE Circular dated 05.11.2002 and then the broker had no such client. The broker further submitted that in November, 2002, when it was introduced in UPSE that Unique Client Code was compulsory for all clients, they complied with the same and hence, no violation had been committed. I am of the view that Unique client code was introduced with the purpose of ensuring that the broker is giving the trade to the client and to know about the amount of exposure of the broker in the securities market in his own capacity. The broker had not produced sufficient proof to substantiate his stand that he had given Unique Client Code to his clients.

4.1.7 Execution of off-the-floor transactions:

The EO found the broker guilty of violating the provisions of SEBI Circular No. SMD/RCG/CIR/(BKG)/293/1995 dated 14.03.1995 and Rule 4(b) of SEBI (Stock Broker and Sub Brokers) Rules, 1992 and provisions of para A(5) of Schedule II specified under Regulation 7 of SEBI (Stock Broker and Sub Brokers) Regulations, 1992 since the broker failed to report the off-the-floor transactions to the Exchange and the broker did not produce any documentary evidence to prove that he reported the same to the Exchange. The broker replied that the circular states that the broker should submit the information of off-the-floor transactions to the Exchange on the same day and it is the duty of exchange to submit the same to SEBI and moreover, the UPSE circular dated 12.08.2002 provided a penalty of 0.01% of the value of transactions on the member concerned if off-the-floor transaction were not reported and later it came to the knowledge of the Exchange. The broker further submitted that since no penalty is levied by the Exchange, it is clear that there is no violation in this regard. I am of the view that the broker had not replied to the point. As per the above circular, the broker had to report off-the-floor transactions to the Exchange and the broker had not produced any evidence that he had reported the same. Only when the non-reporting comes to the knowledge of the Exchange, action can be initiated. Since the broker had not reported, the same would not be in the knowledge of the Exchange and hence, action may not have been initiated till now by the Exchange. Moreover, as per SEBI Circular No.SMDRP/Policy/Cir-32/99 dated 14.09.1999, "*All negotiated deals (including cross deals) shall not be permitted in the manner prescribed in circulars mentioned above and all such deals shall be executed only on the screens of the exchanges in the price and order matching mechanism of the exchanges just like any other normal trade*". The broker had executed off-the-floor transactions which is against the aforesaid provisions. The transactions pertain from the period between April,2001 to March,2003 which is after the passing of the circular dated 14.09.1999. Moreover, the screen based trading was introduced so that there may be greater transparency, better price discovery, reduction in transaction cost and benefits the investors. The off the floor transactions tends to avoid transparency requirements, do not contribute to price discovery and some investors do not have benefit of the best possible price and militate against the basic concept of stock exchanges, which are meant to bring together a large number of buyers and

sellers in an open manner. It is clear from the above circular dated 14.09.1999 that the issue is not of reporting to Stock Exchange as such but execution of such transactions on the Stock Exchange only and not off the Stock Exchange. Hence, I am not inclined to take a lenient view in this regard and hold the broker guilty of violating the above said circulars.

4.2 On a careful perusal of the charges, and the findings as recorded above, I am of the view that a minor penalty of suspension of registration of the broker for a period of 15 days would be adequate and sufficient to have a deterrent effect on the broker.

5.0 ORDER

5.1 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 said Regulations, I hereby impose a minor penalty of suspension of registration for a period of 15 days on Sakshi Stocks and Shares Pvt. Ltd., member, UPSE, bearing SEBI Registration No. INB100858538.

5.2 This order shall come into force immediately on the expiry of twenty one days from the date of this order.

PLACE: MUMBAI

DATE : 15-09-2006

V.K.CHOPRA

WHOLE TIME MEMBER

SECURITIES AND EXCHANGE BOARD OF INDIA