

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA

CORAM: DR.T.C.NAIR, WHOLE TIME MEMBER

**IN THE MATTER OF
SURESH PRABHU K .
MEMBER, BANGALORE STOCK EXCHANGE SEBI REGISTRATION
NO.INB080167613**

DATE OF HEARING : May 15, 2006
APPEARANCES :
FOR NOTICEE : Shri K Suresh Prabhu
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 Suresh Prabhu K (hereinafter referred to as the 'broker') is a member of the Bangalore Stock Exchange (hereinafter referred to as 'BgSE') and is registered with the Securities and Exchange Board of India (hereinafter referred to as 'SEBI') as a broker under Section 12 of SEBI Act, 1992 with Registration Number INB080167613.
- 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 from April 2002 till the date of inspection was conducted. The inspection was carried out by SEBI, on June 20, 2002. During the inspection, certain irregularities found to have been committed by the broker were observed.
- 2.1 An Enquiry Officer (hereinafter referred to as "EO") was appointed vide order dated November 18, 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 (SCN) No. LGL/AB/2003/23915 dated December 17, 2003 was issued to the broker under Regulation 6 (1) of the said regulations. The broker submitted his reply dated January 16, 2004. The enquiry officer conducted the enquiry in terms of the said Regulations and after considering the reply and the submissions made by the broker, the EO submitted his report dated July 5, 2004 recommending suspension of registration of the broker for a period of four months.
- 3.1 A show cause notice dated July 12, 2004, in terms of Regulation 13(2) of the said Regulations was issued to the broker calling upon him to show cause as to why appropriate penalty including the penalty as recommended by the EO should not be imposed on him. The broker replied to the SCN vide letter dated July 27, 2004 stating that he had not received the notice of hearing dated February 18, 2004 from the EO and hence he was not aware of the hearing date. As he had not received the said notice of hearing, the broker sought an opportunity of personal hearing to present his case. Accordingly, the broker was given an opportunity of hearing on August 30, 2004. The broker attended the hearing and also made his written submissions dated September 03, 2004. Subsequently, due to change in the Competent Authority, the broker was given another opportunity of personal hearing on May 15, 2006 on which date the broker appeared and made his submissions.

4.1 I have carefully considered the findings of inspection, enquiry and the submissions made by the broker and find as under :

4.2a) **Non-maintenance of deposit of Minimum Margin by clients**

The EO found that the broker had failed to collect margins from clients which is in violation of SEBI Circular No.SMDRP/Policy/Cir.33/2000 dated July 27, 2000 read with Cir. 6/2001 dated February 1,2001 which requires that all the clients should deposit a minimum margin of not less than 10% of the net open position of a client. I find that in the instant case, the broker has stated that most of the transactions were on his own personal account and that the client transactions were very few and were done only because they were relatives or close friends. I agree with the views of the EO that this contention of the broker cannot be accepted as there is no such exemption from the requirement of maintaining deposit of minimum margin for relatives or close friends. I, therefore, find that the broker has not complied with the SEBI circulars stated above. However, in view of the submissions made by the broker that client transactions are very few and that they were squared up within the same settlement, a lenient view is to be taken.

b) **Non segregation of clients' funds from own funds**

The EO found that the broker had only one account for clients' funds and own funds and had paid certain expenses like telephone bills, rent etc. from this account. The broker submitted that he had not used the clients' account for the establishment expenses and that all such expenses had been met out of his own account. EO found the explanation unacceptable in view of the fact that he had met establishment expenses from the same account in which he was depositing clients' cheques. Hence the EO found the broker guilty of violation of SEBI Circular No. SMDRP/Policy/ Cir/93/23321 dated November 18, 1993 as also the bye-laws of the exchange in respect of client-broker relationship.

I note that the amounts to the credit of clients' accounts are in the nature of trust. The funds in the clients' accounts cannot be applied for any purpose other than what is permissible. The objective of opening and maintaining a separate account for the clients' funds is to segregate and identify them separately and to prevent its misuse so that they are beyond the reach of the broker. Not maintaining a separate clients' account is, therefore, in violation of the provisions stated supra. However, since there is no evidence of using clients' money for his own purposes by the broker as also absence of investor complaints in this regard, a substantive punishment may not be warranted.

c) **Unauthorised carry forward of transactions**

The EO found that the broker had indulged in carry forward transactions as a result of which the scrip recorded an artificial higher rate in the market. The broker stated that the occurrence of carry forward transaction was coincidental and not purposely done. I note from the inspection report that the broker had indulged in carry forward transactions for a successive period of ten settlements. Further the carry forward transactions were done with one particular broker in several scrips. Thus, the transactions as above cannot be mere coincidence as claimed by the broker. By indulging in such transactions the broker had temporarily postponed his obligations towards the exchange in terms of payment or deliveries which goes against the interest of the exchange.

d) **Execution of off the transactions**

The EO found that the broker had executed off the floor transactions and thus violated SEBI Circular dated September 14, 1999. The broker submitted that he had conducted off the floor transactions as a client of the sub-brokers of the BgSE as he was not granted sub-broker registration. The broker has, therefore, admitted that he had executed off the floor transactions. The broker had dealt with about six other brokers and the volume of such transactions ranged between Rs.2.67 lakhs to Rs.1.99 crores. As per SEBI Circular No.SMDRP/Policy/Cir-32/99 dated September 14, 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 to the financial year 2000-01 which is after the issuance of the circular dated September 14, 1999. The screen based trading was introduced so that there is 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 the 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 September 14, 1999 that such transactions are to be executed only on the stock exchange 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 circular.

e) **Registration not obtained with SEBI**

The EO found that the broker had acted as sub-broker and executed trades in NSE and BSE segment through few other brokers of the Exchange without being registered as a sub-broker.

The broker submitted that the registration with SEBI was delayed for the reason that he had not paid the fees though he had actually made the payment and hence requested that the charge may be dropped. The broker has also stated that in view of the delay in registration, he had done some trades on his own account with sub-broker of BgSE as their clients. Though delay in obtaining registration does not authorise the broker to act as a sub-broker without obtaining the certificate, the submission of the broker merits due consideration.

- 4.3 On a careful consideration of the findings of the EO and the submissions made by the broker, as discussed above, and in the facts and circumstances of the case, a minor penalty of suspension of certificate of registration of the broker for a period of fifteen days would be adequate and appropriate.
- 5.1 Now, therefore, in exercise of the powers conferred upon me in terms of Section 19 of SEBI Act, 1992 read with Regulation 13(4) of SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations 2002, I hereby impose a minor penalty of suspension of certificate of registration on Suresh Prabhu K, bearing SEBI Registration No.INB080167613, for a period of fifteen days.
- 5.2 This order will come into force on the expiry of 21 days from the date of this order.

Place: Mumbai

Date: 29.09.2006

T.C.NAIR

Whole Time Member

Securities and Exchange Board of India