

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA

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

IN THE MATTER OF

MCS LTD.

REGISTRAR TO AN ISSUE AND SHARE TRANSFER AGENT

SEBI REGISTRATION NO. INR 000000056

WTM/TCN/MIRSD-DPS2/21/06/07

DATE OF HEARING: 18.04.2007

APPEARANCE:

FOR NOTICEE: Mr. Ramesh Agarwal, Director

Mr. Alok Agarwal, Senior Manager

FOR SEBI : Mr. Rajesh Kumar Dangeti, Asst. General Manager

ORDER

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

- 1.1 MCS Ltd. (hereinafter referred to as "MCS"), a Public limited Company, is registered with SEBI as a Category – I Registrar to an Issue and Share Transfer Agent (hereinafter referred to as RTI) under section 12 of SEBI Act, 1992 with SEBI Registration No. INR000000056.
- 1.2 Inspection of the books of accounts, documents and other records of the MCS, more particularly to ascertain the role played by MCS as the Registrar to the Public Issues with specific reference to some of the public issues and disinvestment process of Oil and Natural Gas Corporation Ltd. (hereinafter referred to as ONGC), Power Trading Corporation of India Ltd. (hereinafter referred to as PTC) and Bank Of Maharashtra Ltd.(hereinafter referred to as BoM), was carried out by SEBI during April-May, 2004. Certain irregularities/contraventions of SEBI Regulations were observed during the said inspection. A copy of the Inspection Report, containing the findings thereof was sent to MCS vide letter dated 04.10.2004 and the reply of MCS was received vide letter dated 05.11.2004.

2.0 Enquiry Proceedings

- 2.1 An Enquiry Officer (EO) was appointed vide SEBI Order dated 04.08.2005 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 MCS.
- 2.2 A show cause notice dated 19.09.2005 in terms of Regulation 6 of the said Regulations was issued to MCS. MCS vide its letter dated 10.10.2005 sought for extension of time and thereafter, vide letter dated 24.10.2005 submitted its written reply.
- 2.3 As per the request of the MCS, an opportunity of personal hearing was given to MCS by the EO on 07.12.2005 which was attended by Mr.P.N.Rao, Director of MCS along with Mr. Ramesh Agarwal, Director and Mr.Ashok Kambli, Asst. Vice President, who made oral submissions reiterating the submissions given in its reply and requested for further time to file its additional reply. The EO granted the same. Vide letter dated 19.12.2005, MCS submitted its additional reply along with copies of 11 exhibits in support of its submissions.
- 2.4 The EO after conducting the enquiry in terms of the said regulations submitted his report on 17.02.2006 and recommended that MCS may be censured for the violations committed by it.

3.0 Show cause notice and the submissions of MCS

- 3.1 A show cause notice dated 12.06.2006 was issued to MCS along with a copy of the enquiry report, in terms of Regulation 13(2) of the said regulations, advising MCS to show cause as to why the action as may be considered appropriate should not be taken against it.

- 3.2 Since no reply was received by SEBI within the specified time of 15 days, a reminder letter dated 07.07.2006 was sent to MCS. MCS vide letter dated 10.07.2006 requested to give a copy of the Show cause notice since it did not receive the show cause notice and requested for extension of time for reply and the request was acceded to by SEBI. Vide letter dated 10.07.2006, SEBI intimated that a copy of the show cause notice dated 12.06.2006 was hand delivered to its representative at 3.35 pm on 10.07.2006 and advised MCS to submit its reply by 24.07.2006. MCS vide letter dated 13.07.2006 submitted its reply along with documents in support of its contentions.
- 3.3 On 21.02.2007, another show cause notice under Regulation 13(2) of the said Regulations was issued to MCS advising MCS as to why the penalty recommended by the Enquiry Officer should not be enhanced. MCS replied vide letter dated 08.03.2007 stating that it had handled 7 issues at the said time and due to sudden change of schedule made by the Government of India, it had to complete the process of basis of allotment by 29.03.2004 instead of 05.04.2004. MCS, further, submitted that the Bankers to an Issue were also affected due to time constraint and unexpected number of applications and gave incomplete, mis-matched reports. It further submitted that errors and mistakes crept in due to the above factors which could not be averted inspite of sufficient infrastructure and adequate and skilled manpower and there was no negligence, default, intentional delay or willful error on its part.
- 3.4 An opportunity of personal hearing was given to MCS on 30.03.2007 vide letter dated 14.03.2007. MCS informing that its Director had to be present in High Court at Calcutta on 29.03.2007 and 30.03.2007 regarding a pending legal matter, requested for another date for hearing vide its letter dated 28.03.2007. Hence, another opportunity was given to MCS 18.04.2007 and the same was availed by it. Mr. Ramesh Agarwal, Director and Mr. Alok Agarwal, Senior Manager attended the hearing and made their submissions on the said date.
- 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 MCS thereto and my findings are as follows:
- 4.2 At the outset, I have noted that as per the workflow of allotment of shares in public issues through book-building offer, the investors submit their applications to the syndicate member who enters the bid details in the Stock Exchange terminals. Upon closure of the issue, the application forms along with the cheques are forwarded to the Bankers to the Issue (hereinafter referred to as BTI) for realization of cheques and further processing of the applications. The BTI then forwards the applications to the RTI along with a statement known as bank schedule and final certificate. The bank schedule contains details like name of applicant, number of shares applied, cheque no., cheque amount etc. BTI also forwards to the RTI details of applications where cheques were dishonoured, so as to prevent allotment to such applications. RTI verifies the physical applications with the data in the bank schedule and does the data entry and also categorizes the applications. This data so entered is once again verified to weed out invalid applications. Further, the RTI subjects the beneficiary details provided in the application form to a validation process after obtaining the details from the Depositories. For the same the RTI provides the beneficiary details of the applicants to the Depositories and the Depositories in turn provide the details as per their records. The RTI verifies the details provided by the Depositories with those captured by them from the application forms and verifies whether the names, order of names etc matches. The validation process is carried out, in order to identify applications with name mismatch, invalid Beneficial owner (BO) and Depository Participant ID (DPID) etc,. Thereafter the basis of allotment is finalized and the final list of allottees is uploaded for corporate action.
- 4.3 SEBI had conducted the inspection into the affairs of MCS on receipt of numerous investor complaints pertaining to the public issues of ONGC, PTC and BoM. There was overlapping of these three mega issues in which MCS had acted as the RTI and the applications received for these public issues exceeded the number of expected applications.
- 4.4 With regard to ONGC issue, the EO found that MCS had uploaded for corporate action the file containing the details on the number of shares applied for by retail investors and Non Institutional Bidders/Investors (HNI), instead of uploading the file containing the details on shares allotted to such applicants as per the basis of allotment. This resulted in the HNIs getting full allotment instead of proportionate allotment and 46,434,810 additional shares were wrongly credited. In respect of retail investors, the file for corporate action was uploaded even before the basis of allotment was finalized and approved by the stock exchange. The RTI had not carried out an independent verification of the details on the application forms with the details of the investors as obtained from the depositories, hence even those who did not apply in the public issue got allotment. In view of the faulty procedures adopted by MCS, the same resulted in basis of allotment being prepared more than once, 3482 applications not being considered for allotment, 1009 applications being considered twice etc,. Further, 11,593 cases of multiple applications received allotment instead of being rejected, in 5,700 cases instead of being rejected allotments were made to applicants where the BO and DPID was not mentioned, 22,320 cases in which PAN numbers were not mentioned received allotment instead of being rejected. EO also found that MCS had allotted ONGC shares in respect of 18 applications of PTC, a mistake which occurred due to mixing up of forms by BTI, however the same should have been verified by MCS before allotting. If the normal procedure had been followed by MCS, this could have been averted. Moreover, in respect of 11,493 applications shares were not credited as on 03.06.2004. There were 5,743 instances where BO and DPID were not captured in data entry, 5,847 cases wherein application number had been entered twice, 75

instances of name field left blank in the application and they were not rejected and 345 instances of wrong application number mentioned. MCS had not dispatched the refund orders and credit of shares to the Beneficiary account and it had not completed them within the specified time of 05.04.2004 and even on the date of inspection, the work was not completed.

- 4.5 With regard to PTC issue, the EO found that MCS had taken the demographic details from the Depositories rather than being entered by manual data entry from the application forms. The prospectus of PTC did not mention that the demographic, bank details would be obtained from the Depositories. This in turn resulted in invalid applications being considered for allotment, shares were allotted against applications where cheques were dishonoured and there were wrong credits/refunds to investors who had not even applied in the public issue, thereby causing opportunity loss to genuine investors. Further, in 435 instances shares were allotted to applicants whose cheques were dishonoured, in 164 instances there was excess/short allotment/refund, 1,800 cases of multiple applications received allotment instead of being rejected, 743 cases in which BO and DPID not mentioned received allotment instead of being rejected, 2,200 cases in which PAN numbers were not mentioned received allotment instead of being rejected. Moreover, in 4,685 cases, refund orders were not delivered since the addresses were downloaded from Depositories instead of manual data entry from the applications and the data of the Depositories were outdated. The EO further found that in 3,471 applications, shares were not credited as on 26.05.2004. There were 3,804 cases where application number had been entered twice, 750 instances of name field left blank and 96 instances where application field left blank and in 285 cases allotment was done to investors who had not applied for it. MCS had not dispatched the refund orders and credit of shares to the beneficiary account and it had not been completed within the specified time of 24.03.2004 and was incomplete as on the date of the inspection report.
- 4.6 With regard to Bank of Maharashtra issue, the EO found that 82,400 applicants got shares in physical format against their preference in demat format on account of improper data entry. Further, 5,800 cases of multiple applications received allotment instead of being rejected, 21 cases in which PAN numbers were not mentioned received allotment instead of being rejected. The EO found that 8,500 applications in a sample of 10,000 did not have bank details but were still allotted shares. MCS had not dispatched the refund orders and credit of shares to the Beneficiary account and it had not completed them within the specified time of 03.04.2004 and was incomplete as on the date of the inspection report.
- 4.7 MCS had admitted in its reply that the applications received were far greater than the expected applications and it was the sole RTI to all these three issues. MCS had admitted in its statement recorded on 26.06.2004 that it invariably outsourced all data entry work to outside agencies. The EO found that the quality of the work outsourced was of very poor quality and MCS did not subject the work of the agents to a verification process due to deadline pressure and paucity of time. As per clause 5(i) of SEBI Circular No. 1(94-95) dated 11.10.1994 *"Keeping the investors interest in mind, RTI/STA shall not accept work disproportionate to its capacity. RTI/STA shall not unload the entire/substantial proportion of its activities to outside agencies except in case of exigencies beyond its control."* MCS has clearly violated the above said provision. I am of the opinion that outsourcing work in exceptional circumstances is allowed. But MCS had accepted work disproportionate to its capacity. MCS had replied that its suggestion to the Book Running Lead Managers (hereinafter referred to as BRLM) to appoint another Registrar was rejected by the Ministry of Disinvestment in the case of ONGC issue and had produced the copy of the proposal in its support. I am of the opinion that instead of doing the work solely, MCS could have insisted for appointment of another Registrar also. Moreover, MCS had admitted in its reply that it had handled four other issues along with these three issues as the sole Registrar which were handled in the month of March, 2004 which shows that MCS had not acted with due diligence and had accepted work beyond its capacity.
- 4.8 MCS in its reply submitted that with regard to ONGC issue the Government of India (hereinafter referred to as GoI) and the other issuers wanted to get the issue proceeds before 31st March, 2004. MCS further submitted that GoI wanted MCS to complete all the formalities before 29th March, 2004. MCS had produced Aggressive Settlement Timeline decided by the Ministry of Disinvestments in due consultation with all intermediaries in support of its contention. It is clear that MCS outsourced its work to its agents without proper control, monitoring and supervision which resulted in poor quality of data entry by the outsourced agencies resulting in large number of errors. Moreover, MCS did not verify the work submitted by the agents which resulted in the above said irregularities.
- 4.9 It is apparent that the consequences of poor quality of outsourcing the data entry work resulted in wide range of irregularities like invalid applications getting allotment, shares were allotted against applications where cheques were dishonoured and there were credit of shares to wrong accounts, dispatch of refund orders to wrong addresses etc.,. Demographic details like address, bank account details of the investors were obtained from the Depositories instead of data entry from physical applications resulting in wrong credits/refunds to accounts since the data with the Depositories was different than the one indicated by the applicants in their application form. Moreover, MCS had admitted that it did not follow the normal procedure for processing the applications in PTC and ONGC issues in its statement dated 24.06.2004. MCS had used the data in the soft copy of the bank schedule instead of making its own data entry from the physical applications due to paucity of time. If MCS had followed the regular procedure, these irregularities could have been averted.

- 4.10 The EO found that in the ONGC issue, MCS had wrongly uploaded the file containing details of shares applied for by both retail and high networth investors instead of retail investors alone resulting in full allotment to high networth investors instead of proportionate allotment. Though the error had been rectified subsequently, MCS cannot deny the fact of the poor quality of work and lack of diligence.
- 4.11 MCS had replied that due to heavy volume and insufficient manpower/infrastructure, some of the Banks, their Branches had failed in their assigned duties and due to gross negligence they had mishandled the applications received by them and as a result did not send the application forms as per the time frame. MCS further submitted that there were discrepancies in the forwarded applications by BTI like PTC applications listed in ONGC issue, PTC application mixed up with Petronet LNG issue, clubbing three categories in ONGC issue viz shareholder, employee and public, resulting in wrong allotment made to investors, discrepancies in bank schedule like duplicate bank serial number, investor name field blank, no bank serial number, bank serial number not matching with the bank serial number given on the application and incorrect bank serial number given as cheque returns. The reply of MCS cannot be sustained, since, if MCS had followed the normal procedures, the irregularities could have been avoided. Also the above lapses on the part of BTIs cannot be attributed by MCS as the reason for their failure. As per the normal procedure to be followed, the RTI should have verified the physical applications with the bank schedule and should have independently done the data entry which should be suitably verified again to weed out any invalid applications. Moreover, MCS had not separately verified the work of the agents, which was outsourced, due to deadline pressure. It is clear that negligence and lack of due diligence had led to these irregularities. MCS should not have deviated from the normal procedure and relied on the bank schedule as admitted by it. I, therefore, hold that MCS had violated clauses 2, 3 and 30 of the Code of Conduct as specified in schedule III of Regulation 13 of SEBI (Registrars to an Issue and Share Transfer Agents) Regulations, 1993.
- 4.12 The EO found that MCS had not redressed the grievances of the investors within the prescribed period of 30 days i.e., complaints pertaining to non-receipt of allotment/refund order. It is clear that if MCS had followed the normal/prescribed procedure for the processing of the application with due care and diligence, these complaints would not have arisen. EO had observed that the investors' grievances had not been redressed within the prescribed period of 30 days in 50 instances in PTC issue, 300 in BoM issue and 344 in ONGC issue. MCS had replied that the delay in redress was due to the fact that the complaints were received late. MCS further submitted that the receipt of large number of complaints was due to the error incurred from the bank schedule and the investor giving incorrect Beneficiary details for which MCS had produced documents. It can be reiterated again that if MCS had followed the prescribed procedure, there could not have been such a chaos in allotment/refund orders. Moreover, the complaints had not been disposed of within the prescribed period of 30 days thereby violating Rule 4(1)(e) of SEBI (Registrars to an Issue and Share Transfer Agents) Rules, 1993 and clauses 5(b) and 21 of the Code of Conduct as specified in Schedule III of Regulation 13 of SEBI (Registrars to an Issue and Share Transfer Agents) Regulations, 1993, and MCS had not given any satisfactory reply on this issue.
- 4.13 I have noted the findings of the EO that the number of applications in electronic book was 30,000 and 20,000 more than the physical applications received for ONGC and PTC issues respectively, an irregularity committed on the part of the syndicate member and the multiple BTI in the book building issue also caused delay since the refund procedure is required to be done separately for each BTI. Apart from the negligence and lack of due diligence of RTI, lack of due skill and care of BTI, BRLM and Syndicate member also added fuel to the problem. Though MCS has stated that there are some mitigating factors like BTI had given incorrect bank schedule, mixed up the applications of the three issues and delayed in dispatching the bank schedule, Co-Registrars to the issue had not been appointed inspite of MCS's request to BRLM, MCS took initiative to pay interest for delayed payment to the investors and set up a call centre to address investors queries arising out of these issues, it cannot be denied that MCS had committed lapses in taking due care and diligence in doing its work which led to the irregularities. In order to protect the interest of the investors and orderly development of the Securities Market, SEBI framed various Regulations and issued Circulars to various intermediaries on various aspects. The intermediaries are expected to abide by the Regulations and Circulars in order to uphold the integrity of the market and to invoke the trust of the investors in the market. If those provisions are not followed strictly by the intermediaries, that cannot be taken lightly.
- 4.14 It is clear that MCS had violated Rule 4(1)(e) of SEBI (Registrars to an Issue and Share Transfer Agents) Rules, 1993 and Clauses 2, 3, 5(b), 21 and 30 of the Code of Conduct as specified in schedule III of Regulation 13 of SEBI (Registrars to an Issue and Share Transfer Agents) Regulations, 1993. In the facts and circumstances of the case, I am of the view that the penalty of censure on MCS for the above said violations as recommended by EO is not adequate. It is desirable to impose a penalty of prohibition of taking fresh business by MCS for a period of 15 days in the interest of investors and the orderly development of the securities market.

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 prohibit, M/s. MCS Ltd., Registrar to an Issue, bearing SEBI Registration No. INR000000056, from taking fresh business for a period of 15 days.
- 5.2 This order shall come into force immediately on the expiry of twenty one days from the date of this order.

PLACE: MUMBAI

T.C.NAIR

DATE : 14.06.2007

WHOLE TIME MEMBER

SECURITIES AND EXCHANGE BOARD OF INDIA