

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA**CORAM: Dr. T.C.NAIR, WHOLE TIME MEMBER****IN THE MATTER OF M/s. P.C.KAPILA & COMPANY, MEMBER OF DELHI STOCK EXCHANGE, INB NO. 050094514**

Date of hearing: July 14, 2006

Appearances:

For Noticees: Shri P.C. Kapila, Proprietor

For SEBI : Shri P.K.Kuriachan, General Manager
Shri Rajesh Gujjar, Asst. General Manager**ORDER****(Under Regulation 13(4) Of SEBI (Procedure For Holding Enquiry By Enquiry Officer and Imposing Penalty) Regulations, 2002 against M/s. P.C.Kapila, Member of Delhi Stock Exchange, SEBI Registration No. 1NB 050094514)****1.0 Background**

- 1.1 M/s. P.C.Kapila & Co. (hereinafter referred to as "the broker") is a member of the Delhi Stock Exchange Ltd. (hereinafter referred to as "the DSE") and is registered with the Securities and Exchange Board of India (hereinafter referred to as "SEBI") as stock broker under Section 12 of Securities and Exchange Board of India Act, 1992 (hereinafter referred to as "the Act") with registration number INB050094514.
- 1.2 SEBI conducted an inspection of the books of accounts, documents and other records maintained by the broker for the period from April 1, 2000 to August 8, 2002 (hereinafter referred to as the "inspection period"), under Regulation 19 of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992 (hereinafter referred to as Stock Brokers Regulations) and the same was carried out by M/s J P Kapur Oberoi & Co. Chartered Accountants on behalf of SEBI.
- 1.3 Certain irregularities/contraventions of SEBI Regulations were observed during the said inspection. A copy of the findings of the Inspection Report was sent to the broker for his comments on April 2, 2003. The broker has replied to findings of the inspection report vide letter dated April 24, 2003.

2.0 Enquiry Proceedings

- 2.1 On completion of inspection, SEBI Board in terms of Regulation 5 (1) of the SEBI (Procedure for holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as Enquiry Regulations) appointed an Enquiry Officer vide order dated December 18, 2003 to examine the irregularities/violations observed committed by the broker.
- 2.2 A show cause notice dated March 18, 2004 in terms of Regulation 6(1) of the Enquiry Regulations was issued to the broker advising it to reply to the allegations within 21 days of the notice. The said notice referred to the inspection report of SEBI in respect of the broker containing the details of violation of various provisions of law.
- 2.3 The broker vide its letter dated April 1, 2004 submitted reply to the aforesaid show cause notice and also requested for personal hearing.
- 2.4 An opportunity of personal hearing before the Enquiry Officer was granted to the broker vide letter dated July 5, 2004 on July 23, 2004 at Regional Office of SEBI at New Delhi. Shri Prem Kapila, Proprietor and Shri S.K. Chopra, Chartered Accountant appeared before the Enquiry Officer and made oral submissions. Vide letter dated July 28, 2004 further submissions were made by the broker. On completion of enquiry, the Enquiry Officer submitted his report dated September 30, 2004 recommending suspension for the period of 3 months.

3.0 Show Cause Notice and Brokers' submissions

- 3.1 Based upon recommendation of the Enquiry Officer, a show cause notice dated October 8, 2004 in terms of Regulation 13(2) of the Enquiry Regulations, advising the broker to show cause as to why the penalty as considered appropriate should not be imposed upon it. A copy of the Enquiry Report was also forwarded to the broker with the said show cause notice. The said show cause notice was served on the broker through DSE.
- 3.2 The broker was asked to submit his reply to the aforesaid show cause notice within 15 days of the receipt thereof. The broker submitted his reply vide letter dated November 3, 2004 and interalia stated as under:
 - (i) The order books were not maintained because the volume of business was very low and orders received on phone were promptly executed and informed to the client. There is no client complaint in respect of wrong execution / non-execution of orders.
 - (ii) They felt that the serial numbers of contract notes had to start everyday and that there was a very little difference between contract notes having a fresh serial number everyday or having running serial number for wider period of one year. P C Kapila has admitted this lapse.

- (iii) The back office software lacked the time stamping on contract notes which was not noticed by the broker. This minor lapse was rectified at later stage. There is no client complaint in this respect.
- (iv) The difference in client codes in some cases occurred only in cases of transactions of clients involving members of the same family. This was due to wrong punching of codes at the time of execution of trade.
- (v) As regards transfer of trade from self trading account to client account, the trades were from the very origin, executed on behalf of the client but due to clerical mistake these were taken in self trading account.
- (vi) As regards unique client codes, they had distinguished between the clients jobbing transactions and delivery transactions by inserting the digit "I" to the code to distinguish such transactions. As this was not acceptable, the broker discontinued the segregation of the transactions.
- (vii) Inadvertently, on two occasions, small amounts were deposited in the client bank account. However they were withdrawn at a later stage, There is no misuse of clients' funds otherwise than for client's transactions.
- (viii) As regards carry forward transactions, there was clerical mistake in intimating more number of shares for badla and hence the excess number so intimated had to be taken in self trading account.

3.3 An opportunity of personal hearing before me was granted to the broker on July 14, 2006 at Regional Office of SEBI at New Delhi. In pursuance Shri P.C.Kapila, Proprietor and Shri Jay Prakash Shaw, Accountant appeared in person and made oral submission.

4.0 Consideration of Issues

4.1 I have carefully examined the facts and circumstances of the case, the inspection report, enquiry report and the submissions of the broker and my findings are as under:

4.1.1 Non maintenance of books of accounts

The enquiry officer found that the order book was not maintained as per SEBI Circular No. SMD/Policy/IECG/I-97 dated February 11, 1997 and also violating provisions of Regulation 17 of the Stock Broker Regulations. I have noted the submissions made by the broker stating that the orders of the clients were received verbally in person or over the phone and these were executed promptly. It was further submitted that the volume of the business was very low and there were no complaints filed against them regarding wrong execution/ non execution of orders. I am of the view that the order book shows the time of placement and execution of the order which is very important from the investors' perspective. The broker is expected to maintain the order book which is an investor protection measure and the broker failed to maintain the order book as provided by the aforesaid circular. I note that the Hon'ble Tribunal in Appeal no. 367 of 2004 in the matter of *Shubam & Co. vs. SEBI* while dismissing the appeal observed as under:

"As per this circular which is binding on all market intermediaries including the appellant, stock brokers are required to maintain some record where the time when the client places an order must be recorded and the same should be reflected in the contract note along with the time of execution of the order. Admittedly, the appellant has not been maintaining any such record which is usually maintained in a register commonly known as order book. Clause 7 of the circular may appear to be innocuous but it is not so and is very important step which the Board has taken to protect the interest of the investors. In a volatile market like ours where the prices of the scrip fluctuate every moment, it is absolutely necessary that a broker should record the time when it receives an order from a client and also the time when the same is executed. If this is not done the brokers could take the investors (their clients) for a ride and make undue benefit for themselves. It is for this reason that the Board has made it mandatory for the stock brokers to maintain such record. Having issued the circular the Board would be well advised in ensuring strict compliance thereof by every stock broker so that the interest of the investors do not get jeopardized."

4.1.2 Contract Notes did not bear Pre-printed Serial Number

The enquiry officer has found that the contract notes issued by the broker did not bear pre-printed serial numbers starting afresh everyday comprising date and serial number and therefore has violated the directives issued by the SEBI vide circular no. SMD/MDP/CIR/043/96 dated August 5, 1996 and also the provisions of Para A (5) of Schedule II of the specified under Regulation 7 of the Stock Broker Regulations. The broker has admitted the lapse occurred on their part and stated that the same has been rectified at the later stage. I am inclined to take a lenient view in this regard.

4.1.3 Time Stamping not done on the Contract Notes

The enquiry officer has found that the contract notes issued by the broker were incomplete in respect of trade number, trade execution and order time thus violating the SEBI Circular no. SMD/POLICY/IECG/I-97 dated February 11, 1997 and DSE circular no. 120/98 dated September 28, 1998. I find that the broker has violated the directives of the aforesaid circular by which brokers were required to maintain record of time of placement of order by the client and reflect the same in contract note along with the time of execution of the order. However I also note that the broker has admitted the same by stating that the back office software procured from a leading software M/s MCS Ltd. lacked the facility of time stamping and the same was unnoticed by them. As there are no client complaints in this respect pending against them, I am inclined to take lenient view.

4.1.4 Difference in Client Code and Transfer of Trades.

The enquiry officer has found that in some cases there was a difference in the Client Account Code as reflected in the record of transactions downloaded from the DSE system as compared with the Sauda Sheet of the broker. Further for settlement no. 2000037, all the trades attributed to their client, Aditya Ajay Brokers Ltd. had originally been executed in their self trading account and later were transferred to the client's account. It was further observed from the client ledger account that all the trades of this client done in financial year 2000 -01 appeared to have been shifted in the same manner. The

broker has admitted the fact of difference in client codes and transfer of trades and submitted that this happened only in case of transactions involving members of the same family and was due to wrong punching of codes at the time of execution of trades. As regards transfer of trade from self trading account to client's account it was submitted that it was clerical mistake and same were rectified. I agree with the finding of the enquiry officer that the broker has apparently violated the provisions of SEBI Circular no. SMDRP/POLICY/CIR/39/2001 dated July 18, 2001 which made it mandatory to all the brokers to use unique client code for all clients. However it is seen that there are no complaints and since no client funds have been misused, I am inclined to take a lenient view.

4.1.5 Unique Client Code

The Enquiry Officer found that the broker was maintaining two client codes for each client based on the nature of transaction i.e. separate ledger accounts were maintained for jobbing and delivery accounts. The broker submitted that they had merely segregated the transactions of the of the client between jobbing and delivery transactions. Unique Client Code was same for every client except for the digit "I" was added to the code to distinguish between the type of transaction. Since this was not acceptable, they discontinued the segregation of the transactions. Apparently the broker has violated the directives of SEBI circular no. SMDRP/Policy/Cir-39/2001 dated July 18, 2001 which makes it mandatory for all the brokers to use unique client codes for all the clients. In view of the satisfactory reply of the broker that this practice has been discontinued as stated by them. I am inclined to take a lenient view in this regard.

4.1.6 Improper Maintenance of Client Bank Account

The enquiry officer found that although the broker was operating separate client accounts for transactions relating to the clients, these accounts had been used on certain occasions for purposes other than those specified and allowed by SEBI which is in violation to the SEBI circular no. SMD/SED/CIR/93/23321 dated November 18, 1993. The broker submitted that that there was no misuse of client bank account. Due to some technical error on two occasions amounts were deposited in the client bank account but these were later withdrawn. I am of the view that the separation of the clients' accounts and the broker's account had been done with a view to preventing any misuse of the clients money by the broker and it is implemented as an investor protection measure. As the broker has admitted the lapse and further rectified it, I am inclined to take a lenient view in this regard.

4.1.7 Non Reporting of off the market transactions

The enquiry officer has found that the broker was not reporting all off the floor market transactions to the stock exchange and has violated the directives issued vide Circular No. SMD/RCG/CIR/(BKG)/293/95 dated March 14, 1995 and DSE circular No. 37/95 dated June 15, 1995 as well as the provision of para A (5) of schedule II specified under Regulation 7 of the Stock Brokers Regulation. The broker submitted that the two transactions stated in the inspection report were not the cases of the off-market transactions. In the first case, the client was not interested in carrying forward the transactions, hence badla transaction was to be done in self trading account. In the second case, the client did not deliver the shares and accordingly the transaction had to be closed with him. The broker further stated that the values of these transactions so insignificant to warrant any notice on part of SEBI to the broker. Taking in to consideration the submission, a benefit of doubt may be given to the broker.

4.1.7 Indulging in Carry Forward Trading

The enquiry officer found that the broker has indulged in carry forward trading. Settlement No. 2000037 revealed that badla transaction done in one client code had been transferred to another client code. Further credit had been given to the short seller (self trading account). The broker submitted that there was a clerical error in intimating more number of shares of badla and hence number so intimated had to be taken to self trading account. On realization of their mistake they rectified the same and gave credit to the respective client account. The broker has also submitted documentary evidence in support of its contention regarding error in intimating quantity of shares for carry forward. I agree with the finding of the Enquiry Officer that since the broker has submitted the documentary evidence in support of its contention and that only a solitary instance of this nature was observed. Therefore a lenient view is taken in this regard.

4.2 On careful perusal of the charges and the findings as recorded above, I agree with the findings of the Enquiry Officer. Further the broker has admitted their lapses with regard to non maintenance of order book, non segregation of client funds, non printing of serial numbers on contract notes and not mentioning order time in the contract notes. I am of the view that a penalty of three months as recommended by the Enquiry Officer would be excessive. I have noted the submissions made by the broker that there was no deliberate intention to violate any of the provisions of the SEBI Act, Rules and Regulations by it. Further that the business at the Delhi Stock Exchange has already stopped for the last few years and therefore they have already suffered heavily in terms of financial viability. I am of the view that a penalty of censure would be sufficient to meet the ends of the justice.

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 'Censure' M/s P.C.Kapila & Company, Member of Delhi Stock Exchange, to the effect that the broker should be careful in future in conduct of its affairs as a capital market intermediary. I also direct P.C. Kapila to note that any instances of violation or non-compliance of the SEBI Act and Rules and Regulations in future shall be dealt with stringently.