

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

DIRECTIONS UNDER SECTIONS 11(1), 11(4) AND 11B OF THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 TO BARCLAYS BANK PLC .

1. Barclays Bank PLC (hereinafter referred to as 'Barclays') registered as a Foreign Institutional Investor (hereinafter referred to as 'FII') with Securities and Exchange Board of India (hereinafter referred to as 'SEBI') having registration No.IN-UK-FD-0693-01, under the Securities and Exchange Board of India (Foreign Institutional Investors) Regulations 1995 (hereinafter referred to as FII Regulations). Regulations 20A of the FII Regulations casts responsibility on registered FIIs to provide information about Offshore Derivative Instruments (ODIs)/ Participatory Notes (PN) to SEBI in the manner and in the format as prescribed by SEBI. Regulation 20A of FII Regulations provides as under:

“20A. Foreign Institutional Investors shall fully disclose information concerning the terms of and parties to off-shore derivative instruments such as Participatory Notes, Equity Linked Notes or any other such instruments, by whatever names they are called, entered into by it or its sub-accounts or affiliates relating to any securities listed or proposed to be listed in any stock exchange in India, as and when and in such form as the Board may require.”

2. SEBI had also issued circulars under Section 11 of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as SEBI Act) specifying the format for the periodical submission of the information by all

registered entities about their ODI activity. From the reports submitted by Barclays during the period between January 2006 and January 2008, SEBI observed that Barclays had issued four ODIs dated December 15, 2006 with maturity upto May 4, 2011 to UBS AG, with Reliance Communications Limited as the underlying. On perusal and scrutiny of the said reports, SEBI vide electronic mail dated September 24, 2009 had sought the following specific information with respect to the above mentioned four ODIs:-

- a. Date of Redemption
- b. Full or Part of ODI issued (In case redemption has taken place in parts, the details for each part redemption separately).
- c. Quantity Redeemed
- d. Value (in USD)
- e. Value (in INR)
- f. Details of Underlying trades in Indian market with respect to each instrument – in cases of both issuance and redemption of ODI:
 - I. Date
 - II. Sale/Purchase
 - III. Quantity
 - IV. Value

3. In reply, Barclays vide e-mail September 25, 2009 had stated that there were other ODIs which were issued during the two year period January 2006 to January 2008 with the same underlying scrip to the same counterparty for which SEBI was seeking information. Thereafter, Barclays was advised to submit the said information, vide SEBI e-mail dated September 26, 2009. Pursuant to the same, Barclays vide e-mail dated September 28, 2009, submitted the information about fourteen other trades with the same counterparty. It was observed that the said trades were not part of the periodical filings made by Barclays. As the information provided by Barclays was not

complete, SEBI vide e-mail dated November 13, 2009, advised it to furnish information on all ODIs issued to counterparty UBS AG with Reliance Communications Limited as the underlying for the period beginning November 2003 upto October 2009. Further, SEBI had also sought evidential documents in support of the ODIs which were issued to UBS AG with Reliance Communications Limited as underlying. Barclays was advised to submit the said information on or before November 17, 2009. In response, Barclays vide e-mail dated November 17, 2009 stated that in reviewing the documentation with respect to those ODIs, they have identified some discrepancies which were being reviewed by it. Subsequently Barclays, vide e-mail dated November 18, 2009 submitted that upon review, the counterparty of the transactions was not UBS AG as earlier reported by it but was Hythe Securities Limited (hereinafter referred to as Hythe), an entirely new entity which did not form part of any of the earlier periodical submissions made by Barclays to SEBI either in its monthly reports or in the specific information submitted in response to the query with reference to Reliance Communications Limited. Barclays claimed that they were undertaking a review of the reporting and sought confirmation from SEBI whether SEBI still required the evidentiary documents in support of those trades.

4. Thereafter, SEBI vide e-mail dated November 19, 2009 advised Barclays to provide all evidentiary documents in support of those specific trades. Further, Barclays was also advised, vide e-mail dated November 20, 2009 to explain its stand on the wrong information in respect of the ODIs which had been issued, and was further advised to explain, why appropriate action should not be taken against it for the alleged contravention of the code of conduct specified in Regulation 7A of the FII Regulations, which prohibits an FII to make any untrue statement or suppress any material fact in any documents, reports or information furnished to the SEBI.

5. Barclays in its e-mail dated November 23, 2009 requested extension of time to submit the information as required by SEBI. Accordingly, it was granted time up to December 8, 2009. SEBI further clarified in its e-mail dated November 26, 2009 that information sought by it vide e-mail dated November 19, 2009 was required only in respect of Reliance Communications Limited as the underlying. It was further advised to reconcile records for the beneficial owners of all the ODIs reported to SEBI and confirm to SEBI that there are no further re-statements required in the matter. Barclays submitted the information, vide e-mail dated December 2, 2009. As regards the information about the ODIs issued with Reliance Communications Limited as the underlying scrip, Barclays mentioned that it had issued such ODIs only during the period August 2006 to November 2008 and that it had not issued any ODI with the said underlying before August 2006. Further, it furnished information for the specified period for the underlying Reliance Communications Limited. It was observed from the information submitted by Barclays that the ODIs under reference were issued to Hythe and that they were onward issued to another entity Pluri Emerging Companies PCC Cell E Emerging Markets Growth Fund (hereinafter referred to as 'Pluri'). As per the requirement stipulated for PN reporting, all FIIs were mandated to provide the following information on investors to which ODIs are issued :-

	A	B	B1	C
Sr. No.	Name and Location of the person to whom the Offshore Derivative Instruments are issued.	Name and Location of other person in case back to back Offshore Derivative Instruments has been issued against the instrument mentioned in A	Name and jurisdiction of the Regulator by whom the person holding the Offshore Derivatives Instruments, is regulated in terms of Regulation 15 A of SEBI (FII) Regulations, 1995	Type of the investor (e.g. hedge funds, corporate, individual, pension fund, trust etc) This information should be given for column 'B', in case column 'B' information is Nil furnish information for column 'A'

The Report requires FIIs to specify the name and location of the entity to whom ODI is issued in column A. The name and the location of the entity in case the ODI is onward issued back to back to another entity was to be reported under Column B. Column B1 requires the FIIs to provide the information about the regulated status of the entity to whom the ODIs have been issued including the jurisdiction, the regulator with whom the entity is regulated.

6. From the above, it is evident that FIIs are required to provide the name of the investor in case the ODI issued by it is onward issued by the subscriber to any other entity as a back to back instrument. From the monthly reports submitted by Barclays since 2006 with respect to Reliance Communications Limited as the underlying, it was observed that the name of the subscriber was UBS AG which has now been restated as Hythe Securities Limited. Further it was also observed that there has been no back to back issuance of the ODI to any other entity as the column B in the monthly reports are "N/A" (not applicable) meaning thereby that there was no onward issuance of the ODI to any other entity other than what was represented in the reports. However, on perusal of the information submitted by Barclays on December 2, 2009, it was observed that those ODIs were issued back to back to another entity Pluri. In this regard, Barclays has submitted that the Hythe Securities Limited is a regulated entity with the Financial Services Authority, United Kingdom and thus complies with the definition of an appropriate foreign regulatory authority in terms of Regulation 15A(1)(a) of the FII Regulations.

The said provision as on February 3, 2004 states as under:-

"15A. (1) A Foreign Institutional Investor or sub account may issue, deal in or hold, off-shore derivative instruments such as Participatory Notes, Equity

Linked Notes or any other similar instruments against underlying securities, listed or proposed to be listed on any stock exchange in India, only in favour of those entities which are regulated by any relevant regulatory authority in the countries of their incorporation or establishment, subject to compliance of "know your client" requirement:

Provided that if any such instrument has already been issued, prior to 3rd February 2004, to a person other than a regulated entity, contract for such transaction shall expire on maturity of the instrument or within a period of five years from 3rd February, 2004, whichever is earlier.

(2) A Foreign Institutional Investor or sub account shall ensure that no further down stream issue or transfer of any instrument referred to in sub-regulation (1) is made to any person other than a regulated entity."

The said provision as amended with effect from May 22, 2008 is as under:

(1) No foreign institutional investor may issue, or otherwise deal in offshore derivative instruments, directly or indirectly, unless the following conditions are satisfied:

(a) such offshore derivative instruments are issued only to persons who are regulated by an appropriate foreign regulatory authority;

(b) such offshore derivative instruments are issued after compliance with 'know your client' norms:

.....

(2) A foreign institutional investor shall ensure that no further issue or transfer is made of any offshore derivative instruments issued by or on behalf of it to any person other than a person regulated by an appropriate foreign regulatory authority.

7. It was provided in the FII Regulations that those ODIs which were issued to persons not satisfying the criteria as on 2004, would be liquidated over a period of five years ending 2009, and fresh ODIs could not be issued except in compliance with the said regulations. Thus the underlying principle in the regulations was that the ODIs could not be issued or subscribed by any entity that is not regulated by an appropriate foreign regulatory authority after February 2004. From the information provided by Barclays, it is evident that the ODIs which were issued by it to Hythe Securities Limited (originally stated to be issued to UBS AG) were subsequently issued to Pluri, prima facie in contravention of Regulation 15A(2) of the FII Regulations. It is also pertinent to note that the ODIs were issued afresh after the amendment to the regulations inserting regulation 15A in February 2004. FII Regulations casts responsibility on an FII to ensure that any downstream issuance of ODIs is in strict compliance with the FII Regulations. As mentioned above, it is evident that Barclays was aware that the ODIs issued by it to Hythe Securities Limited were onward issued to Pluri. However, Barclays has continued to misrepresent to SEBI that the ODIs were not issued "back to back" to any other entity, by providing monthly reports with column B1 (as mentioned in the table above) "not applicable". This shows the blatant disregard by Barclays in complying with the provisions of the FII Regulations. Barclays, vide e-mail dated December 2, 2009 acknowledged that the details of the ODIs were wrongly reported to SEBI due to manual compilation of the ODI reports in December 2006 and error in data entry level. Barclays further submitted that after improvements in its systems for ODI reporting in 2008 and 2009, the errors in reporting continued to be carried forward in the new system. It is also observed that Barclays acknowledged that even in November 2009, when further information was requisitioned by SEBI, it failed to identify the true counterparty for those trades. Barclays has also submitted that it would ensure that necessary resources are

allocated to ensure that the reports submitted to SEBI are adequately re-examined prior to its submission.

8. It is also brought to my attention that in the past too, there were a few occasions which should have prompted Barclays to have a relook at their reports submitted to SEBI through their reporting platform. These were after the supposed implementation of the new reporting platform claimed to have been put in place by Barclays. At least on two occasions in the not so distant past, SEBI vide e-mails dated January 16, 2008 and again on July 3, 2008 had required Barclays to provide certain basic information which was critical for the assessment of the ODI activity undertaken by it. These prompts would have cautioned Barclays to review the ODI reports submitted to SEBI. However, Barclays did not do so and continued to provide false and incorrect information to SEBI. As regards the issuance of ODIs downstream to Pluri, Barclays has stated that the Memorandum of Understanding (MoU) signed by it with Hythe dated November 7, 2006 provided an ability for Barclays to seek information on the end beneficiary owner of the ODI so issued. However, given that Barclays was aware that the ODIs were onward/ downstream issued to an unregulated entity, it failed to comply with the regulations governing ODIs and provide correct and true picture of the ODIs issued by it.

9. I am therefore of the opinion that Barclays has not only failed to provide true, fair and complete details of the ODI activity undertaken by it but also prima facie violated the provisions of FII Regulations by furnishing false and incorrect information to SEBI. Full and fair disclosure forms the cornerstone of FII regulation by SEBI. As the source of funds available with an FII comes from Offshore, by its very nature SEBI has no direct access to verifying the nature of the funds or whether the funds will be misused for the purpose of market manipulation or for perpetrating any type of fraud in the market. The very

essence of the amendments to the FII regulations in Regulations 15A and 20A reflects this pressing regulatory concern on the part of SEBI. In other words, SEBI places almost absolute faith and unqualified reliance on the ability of an FII to carry out the basic regulatory and prudential oversight. Once this faith is violated and the integrity of the process vitiated, then FII inflows can potentially become conduits for large scale manipulation and fraud in the market. Therefore, SEBI as a regulator requires fair, true and correct information for assessing and monitoring FII activity in the securities market. When a registration is granted to an FII, SEBI presupposes that the FII has the capacity to exercise the necessary oversight and ensure the integrity and accuracy of the data it provides to SEBI under the regulations applicable. It appears that, from the facts discussed above, Barclays has been non compliant with the provisions of the regulations and is not capable of providing such information. As a regulator therefore, SEBI cannot allow such an entity to continue with any activity with regard to ODIs. After due consideration of the facts and circumstances of this case, I am of the view that Barclays needs to be restrained in its activity in dealing with ODIs till such time as SEBI is satisfied that Barclays can provide true, accurate and complete picture of its ODI transactions as envisaged by the FII regulations and the reporting requirements therein. Therefore, I find it necessary, in order to protect the interest of the investors and for the orderly development of the securities market to take preventive measures and issue urgent directions in this regard to ensure that such kind of violations do not continue or get repeated to the detriment of the investors.

10. Accordingly, in exercise of the powers conferred upon me under Sections 11(1), 11(4) and 11B of the Securities and Exchange Board of India Act, 1992, I hereby direct Barclays Bank PLC not to issue/subscribe or otherwise transact in any fresh/new Offshore Derivative Instrument till such time

as Barclays satisfies SEBI that it has put adequate systems, processes and controls in place to ensure true and correct reporting of its ODI transactions to SEBI. Barclays shall furnish a certificate from an auditor of international standing to this end.

11. This order may be treated as a Show Cause Notice and Barclays may, if it so desires, submit its reply on or before December 18, 2009 and may also avail an opportunity of personal hearing in the matter at 3.00 p.m. on Wednesday, December 23, 2009 at SEBI Bhavan, Bandra Kurla Complex, Mumbai 400051.

12. This order shall come into force with immediate effect.

DR. K. M. ABRAHAM
WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA

PLACE: MUMBAI

DATE : DECEMBER 9, 2009