BEFORE THE SECURITIES APPELLATE TRIBUNAL

MUMBAI

APPEAL No.22/2003

Radar Securities Ltd., **Appellant**

Vs.

Securities & Exchange Board of India **Respondent**

Present

Shri Bharat Merchant

Advocate

Shri Utpal Joshi,

Advocate **For Appellant**

Shri Ananta Barua,

Jt. Legal Adviser, SEBI

Shri Santosh Shukla,

Asstt. Legal Adviser, SEBI **For Respondent**

ORDER

The Appellant is a stock broker registered with the Respondent. It is a member of the National Stock Exchange of India Ltd. (NSE). The Respondent carried out inspection of the books of account, and other records of the Appellant some time in November 2000. The inspection revealed the following shortcomings:

(i) failure to maintain Margin Deposit Book under regulation 17 of the Securities and Exchange Board of India (Stock Broker and Sub-broker) Regulations, 1992 (the Stock Broker Regulations).

(ii) Delay in making payment to the clients

(iii) Failure to obtain acknowledgements from clients on the Contract Notes, failure to affix stamps and disclose the order receipt time, on the Contract Notes.

(iv) Incomplete client registration form

(v) Dealt with unregistered sub brokers.

(vi) Made off-the-floor transactions without reporting the same to NSE.

The Respondent forwarded a copy of the inspection report and obtained the comments of the Appellant on the findings of the inspection and thereafter decided to enquire into the affairs of the Appellant. An enquiry officer was appointed on 24.6.2002 for the purpose. The enquiry officer submitted his report to the Respondent on 31.10.2002. The enquiry officer confirmed the findings of the inspection, except the charge of delay in making payment to the clients. He recommended that the certificate of registration of the Appellant be suspended for a period of six months. The Respondent considered the enquiry report and in terms of regulation 13(2) of the Stock Broker Regulations, issued a notice to the Appellant with a copy of the enquiry report, to show cause as to why the penalty as recommended by the enquiry officer should not be imposed upon it. The Appellant responded to the said notice by making written reply followed by oral submissions. The Respondent thereafter issued the impugned order on 10.1.2003. By the said order the certificate of registration granted to the Appellant was suspended for a period of 6 months . The order was to come into operation after three weeks from the date of the order. The Appellant claiming to be aggrieved by the said order filed the present appeal. The order though dated 10.1.2003 and was to be effective after three weeks, was communicated to the Appellant by the Respondent's office vide its letter dated 27.2.2003 informing that the suspension will come into effect from 3.3.2003. The Appellant filed the appeal on 3.3.2003 with an urgent application praying for an interim order staying the operation of the impugned order during the pendency of the appeal. The parties were heard on the said prayer and after considering all the relevant aspects an interim order was passed on 3.3.2003 staying the operation of the impugned order for a period of eight weeks.

Shri Bharat Merchant, learned Counsel appearing for the Appellant submitted that the Appellant has not committed any serious violation of the Act or any rules or regulations so as to warrant such a harsh punishment of suspension of its certificate of registration for six months. He submitted that the charges are not scrip driven but procedural lapses of technical nature of not any adverse consequence on investor interest. Learned Counsel submitted that by the impugned order only the certificate of registration granted to the Appellant as stock broker was cancelled. But the letter dated 27.2.2003 whereunder the order was forwarded to the Appellant has expanded the scope of the order by stating that on and from the date of the suspension, the Appellant will cease to carry on any activity as an intermediary during the period of its suspension. He submitted that the Appellant was holding a certificate of registration to carry on the activities of Portfolio Manager also for the period from 16.3.1995 to 15.3.2001 that no enquiries have been made against the Appellant in its activities in the Scheme of Portfolio Management Services.

Shri Merchant described the profile of the Appellant that it is carrying on stock broking business since January, 1996, that it was holding Portfolio Management Licence during the period16.3.95 to 15.3.2001, that it is also registered as trading member since 2nd June, 2000 and as a Self Clearing Member since 5.7.2002. According to the learned Counsel it is servicing more than 3500 clients registered with it, that it has 10 branches, that issued about 80,000 Contract Notes per year, that no investor complaint is pending and during the course of its tenure of 7 years only 8 complaints had been received and none of them is pending.

Learned Counsel referred to the impugned order and stated that the Respondent had leveled the following charges against the Appellant:

(A) Not maintaining the Margin Deposit Book

(B) Violation of certain requirements with respect to Contract Notes.

(C) Acceptance of incomplete client registration form

(D) Dealing with unregistered sub brokers.

(E) Non reporting of, Off-the-market transaction

Shri Merchant submitted that the Respondent has gone on record holding the Appellant guilty of having violated the provisions of Clauses A(5) and B(1) of the Code of Conduct as specified in the Stock Broker Regulations, regulation 17(1)(k) of the said regulations and rule 4(b) of SEBI (Stock Broker and Sub-broker) Rules, 1992 and directives given by the Respondent.

As regards charge of non maintenance of margin deposit book, learned Counsel submitted that the Appellant had not collected any margin from its clients and therefore the margin deposit book was not required to be maintained. He submitted that, regulation 17(1) requires every stock broker to keep and maintain books of accounts, records and documents specified thereunder, that one of the books to be maintained as per clause (k) thereunder is margin deposit book. He submitted that the circular dated 18.11.1993 relied on by the Respondent is on the requirement of margin collection, that in the present proceedings non collection of margin is not a charge against the Appellant. It was further submitted that in respect of margin paid to the Exchange there is a facility of Electronic Down Load and a seperate file maintained for such margin down load by the Appellant. He submitted that even though technically viewed, margin deposit book was not maintained in physical form, the requisite data was available on the computer, as put in by BSE and at any point of time the data was available and the data provided by BSE could be considered more authentic and tamper proof, that the purpose of maintaining the book is to keep the relevant information and the said purpose has been achieved. Learned Counsel submitted that the fact that Respondent has not prescribed any format for the margin deposit book itself indicates that it is not a crucial register/document, that the failure to maintain such a register in a book form is only a minor technical lapse and such a technical lapse of no consequence does not warrant a major penalty of suspension of the certificate of registration.

With reference to the alleged violation of the provisions relating to Contract Notes, learned Counsel submitted that the Appellant had issued Contract Notes to all its clients, that it had issued about 8000 Contract Notes during the relevant period that not even a single complaint has been received alleging failure on the part of the Appellant to issue Contract Notes to its clients in respect of the transactions carried out on behalf of the clients. He submitted that the purpose of the Contract Note is to record the arrangement between the broker and the client and the purpose of acknowledgement of the Contract Notes by the client is to evidence receipt thereof by the client, and as there being no dispute as to whether Contract Notes have been issued to concerned clients, the purpose having been served there was no violation of the circular dated 5.8.1996 in not having the acknowledgement of client on each Contract Note. Learned Counsel referred to the circular dated 5.8.96 and stated that it is in the context

of certain common irregularities/deficiencies noticed during the course of inspection of the records of brokers of various exchanges that what is highlighted therein include "non maintaining of copies of Contract Notes and maintaining counterfoils of Contract Notes without adequate details" that the requirement therein is that "all Trading Members shall issue Contract Note for purchase/sale of securities to a constituent within 24 hours of the execution of the contract" and "to keep duplicate of the Contract Notes issued by the Members to the constituents". In this context he referred to regulation 17 (1)(i) of the Stock Broker Regulations and submitted that the requirement thereunder is also to maintain "counterfoils or duplicates of Contract Notes issued to clients," that this statutory requirement has been complied with. He submitted that in few cases the Appellant could not get the signature of the clients on the counterfoil of the Contract Notes and this was not a wilful lapse or default on its part, that in any event obtaining of client acknowledgement on duplicate Contract Note is not a mandatory requirements. Learned Counsel submitted that failure to comply with requirements as per the Respondent's circular dated 5.8.96 in few cases is merely a technical violation which has not affected the interest of investors or the functioning of the securities market to warrant a major penalty like suspension of certificate of registration.

With reference to the allegation that stamps have not been affixed on Contract Notes in violation of SEBI circular dated 29.10.1993, learned Counsel submitted that in so far as cases where stamps have not been affixed on the Contract Notes, the said default was not wilful or deliberate and no penalty is imposable for such unintentional failure of no consequences.

Regarding the alleged failure to stamp the timing of orders received, on the Contract Notes learned Counsel submitted that there are practical difficulties in having time stamping of orders done on all the orders placed on the Appellant, that the enquiry officer had also admitted the practical difficulty involved in this. He submitted that since the Appellant is transacting in the NEAT System, the time automatically gets stamped for placement of the order, modification or cancellation of the order and execution of the order. He further submitted that as far as the Appellant is concerned such a requirement is not specified on the specimen form of the Contract Note devised by NSE, that the Appellant is dealing with the transactions on the NSE, and on the NSE approved forms and there is no space for time stamping for placement of order, that while the requirement may exist as per the circular dated 11.2.1997, the same cannot be carried out unless the NSE forms in the first instance is amended, further that back office software is also not available in the market to record the time of placement of order on Contract Notes. He further submitted that in any case the time of order execution is even now recorded on the Contract Notes, and that the time of placing the order is in any case known to the clients.

Referring to the charge that the client registration forms were found incomplete, Shri Merchant submitted that as far as possible the Appellant obtains all particulars from the client and reflect them in the client registration form. With reference to the Respondent's charge that details of client number, GIR number and PAN number were not furnished in the client registration form, the learned Counsel submitted that filling up such details is not mandatory and hence there was no violation of any statutory provisions. He further submitted that as required by the enquiry officer, the Appellant has already complied with the requirements and submitted the same to the Respondents during the personal hearing on 1.1.2003 along with the Appellant's letter dated 24.12.2002, that the Respondent has not considered the fact of compliance. With reference to the charge that in respect of two clients, the proof of identity was not indicated, the learned Counsel submitted that the said clients are traceable, identifiable and

reachable in case of necessity and therefore the deficiency in these two clients' form is not such as to have any consequence on the trade or recovery, that in any case the proof of identity has since been submitted to the Respondent along with the Appellant's letter dated 24.12.2002. With reference to the failure to get the PAN No. disclosed in the form, it was submitted that none of these clients is a defaulter and therefore the omission to fill up the said particulars is merely technical. He further submitted that as per the Respondent's circular dated 11.4.1997 the disclosure requirement of particulars regarding PAN No. and annual income can be waived. He submitted that out of several thousands of client registration forms handled by the Appellant only in 5 cases the enquiry officer had noticed incomplete information, that in the case of one client the observation is that 'the proof of identity of the client is not kept', in another case it has been stated that "Photo and proof of identity/residence missing" that in the remaining three cases the deficiency is "not mentioning annual income and Income Tax PAN Number" – that failure to obtain these particulars in 5 cases cannot be a ground to attract a harsh penalty of suspension of registration certificate.

Shri Merchant stated that another charge which the Respondent has leveled against the Appellant is that of dealing with unregistered sub brokers that according to the Respondent transactions have been carried out with members of Calcutta Stock Exchange, who were neither registered as remisiers with NSE nor were they registered as sub brokers with the Respondent which is in violation of SEBI circular dated 31.3.1997. He referred to the entities with whom the Appellant had transaction – these are (i)VPT Securities (ii)Pawan Deora (iii)Sadasuk Kabra (iv) Kamani Stock Broking Services P. Ltd. and (v) G. M. Pyne. Learned Counsel submitted that Kamani Stock Broking Services P. Ltd. was trading with the Appellant on its account and not for its clients and not as a sub broker or as a remisier, that there was no reason to disbelieve or disregard such confirmation and there was no material available to the contrary. He further submitted that in respect of the other four entities referred to in the enquiry report, the Appellant had raised bills, Contract Notes and issued cheques only in the names of the said entities and all orders were executed on the NEAT system in their name and code only. The same clearly establishes that the Appellant had dealings with such entities not as their sub broker. Learned Counsel submitted that the Appellant was not in a position to know and could not have been known as to whether Pawan Deora & Co., VPT Securities (P) Limited, G.M. Pyne were trading for themselves or on behalf of their clients as the Circulars relied upon and referred to in the enquiry report clearly puts the onus on the sub-brokers themselves to obtain registration with SEBI. Shri Merchant submitted that no case has been made out of the Appellants having wilfully and deliberately entered into transactions with the said entities knowing that they were not trading on behalf of themselves but were trading on behalf of their clients. He submitted that the enquiry officer's finding that Pawan Deora & Co., VPT Securities (P) Limited and M/s. G. M. Pyne were acting as unregistered sub-brokers of the Appellant and unregistered remisiers of NSE is based on surmises and conjectures. He submitted that the size of volumes traded by such entities or the fact of their being members of the Calcutta Stock Exchange Association Limited, could not in any manner lead to the conclusion that such entities were trading not on their own account, but for their clients, that it was common for members of other Stock Exchanges to act on their own account in significant volumes for jobbing, arbitrate, investment and trading. He submitted that the SEBI Circular dated 31.3.1997, in any event, had not been communicated to the Appellant by NSE.

According to the learned counsel there was no way to ensure that clients transact with the Appellants only for themselves and not for any other persons, that Appellant had therefore taken care to warn investors from dealing with any of the Appellant's clients, and had inserted advertisements in leading newspapers in Calcutta on 19/03/2001 and 15/01/2002 to inform investors that the Appellant has

no agents or sub-brokers and hence they should not deal with any of the Appellant's clients under the belief that they are the Appellant's sub-brokers. He submitted that in any event, the violation, if any, of the SEBI Circulars referred to above and in the order is merely a technical violation, that there has been no deliberate or willful violation of the said Circulars by the Appellant and violation, if any, of the same has not adversely affected the interest of any investors in securities nor has it in any manner obstructed the promotion of the development of the securities market or the regulation thereof. According to the learned Counsel the Respondent has appointed NSE as a Nodal Agency for disseminating the circular of the Respondent, that this particular circular dated 31.3.1997 was never circulated by the NSE, that it is not the obligation of the broker in such a case to search the website of the Respondent for every circular issued by the Respondent, that in these circumstances, the question of the Appellant being penalized for not observing an undisseminated circular does not arise.

Referring to the charge of not reporting off-the-market transactions, learned Counsel submitted that the off-the-market transactions referred to in the order were to the tune of Rs..15.07 lacs only as against the Appellant's turn over of Rs.1987.54 crores for the period of April 2000 to November 2000 and thus formed an insignificant share of the Appellant's total turnover, that the said transactions involved small lots of shares in different companies at different times and could not have and did not in any manner prevent the investors from having the benefit of best possible price and did not cause loss to any investor and did not avoid transparency requirements nor did the same militate against the basis concept of NSE and there was no violation of circular dated 14.9.99 as alleged. He submitted that in any event the violation, if any, of the said circular is merely technical, and was not deliberate or wilful and/or did not in any manner affect the interest of the investors or the securities market.

Learned Counsel submitted that penalty of suspension of the Appellant's certificate of registration for a period of six months is not justified. He submitted that most of the submissions made by the Appellant remain uncontroverted. According to him the conditions prescribed in Regulation 13(6) of the SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 have not been fulfilled in this case and as such "Major Penalty" cannot be invoked. He submitted that the violations complained of as against the Appellant are merely technical in nature and have not adversely affected the interest of any investors in securities nor have it in any manner obstructed the promotion of the development of the securities market or the regulation thereof. According to him when considered against proportionality of the violation even major penalty cannot be imposed.

Learned Counsel submitted that there is no nexus between the alleged charges and the level of penalty imposed, that it is well settled that penalty must bear relevance to offence charged, that all the violations referred to by the Respondent are domestic violations, insignificant, technical, inadvertent or through oversight and no penalty is warranted in the facts and circumstances as put forth by the Appellant. In this context learned counsel referred to the Hon'ble Supreme Court's decision in Hindustan Steel Ltd. V State of Orissa and this Tribunal's observation in Escorts Mutual Fund V Shri Sai Ram (2002) 35 SCC 918) and Cabbot International Corporation v Adjudicating Officer (2001) 29 SCL 399) to support his submission that penalty per se the violation is not permissible, that imposition of penalty is justified only if it is established that the failure to carry out a statutory obligation was an act deliberately in defiance of law or was guilty of conduct contumacious or dishonest or acted in conscious disregard of its obligation, that in the Appellant's case the failure was only a technical failure.

Shri Merchant referred to this Tribunal's observation in M.J.Patel V SEBI (2002)38 SCL 889) that "suspension or cancellation of the certificate granted to carry on broking business is not a matter which could be treated lightly" and submitted that in the absence of sufficient justification supported with reasonable evidence, such a penal action cannot be sustained. He submitted that the Respondent has failed to provide sufficient justification for imposing the penalty of suspension of the certificate of registration.

He submitted that suspension of certificate of registration, in the Appellant's case would lead to closure of business and cause severe damage to its reputation, that suspension of the Appellant's registration would also result in the Appellant's clients moving to other firms during the suspension period and could also result in employees of the Appellant being left without employment.

Shri Ananta Barua, learned representative of the Respondent submitted that an inspection of the books and records of the Appellant was conducted by the Respondent some time in November 2000 which revealed some irregularities committed by the Appellant, that the inspection report was made available to the Appellant for its comments and on receipt of the comments, the Respondent prima facie felt the need to enquire into the matter and for the purpose an enquiry officer was appointed, that the enquiry officer on completion of the enquiry submitted his report. He submitted that for the purpose of inspection a particular period is chosen and the compliance is verified within that specific period as it is practically impossible to cover several years, that the records etc. are also chosen for inspection on a sample basis, that therefore it does not mean that violations/deficiencies were confined only to the few instances against the large number of transactions carried out or documents maintained. He submitted that the Appellant has not disputed the factual position revealed in the enquiry report, that its only grievance is that the omissions and commissions are not that serious to warrant penalty of suspension of the certificate of registration.

Shri Barua submitted that the Appellant in response to the findings in the inspection report, vide letter dated 14.2.2001 has stated that the margin deposit book has been kept by keeping the margin statements down loaded from NSE system in a serial order, that in its subsequent letter dated 20.9.2002, it has been stated that "we have not collected any margin. Hence it was not required" to maintain Margin Deposit Book. He submitted that down loading data from the stock exchange system is not a substitute for maintaining the book by the broker, that the margin deposit book is an important document, and it is required to be maintained as per regulation 17(1)(k) of the Stock Broker Regulations. He submitted that as per the said regulation every broker is required to keep and maintain margin deposit book and for the failure to comply with the said requirement penalty has been provided in the regulation.

Shri Barua submitted that it is a requirement of regulation 3.5 of NSE Regulationsthat the member broker shall issue Contract Note for purchase/sale of securities, to clients within 24 hours of the execution of the Contract Note as specified by NSE, that the Contract Note as specified by NSE requires maintaining trade time and affixing of stamp as required under the Stamp Act. Learned representative referred to the format of the Contract Note forming part of the reply and submitted that there is specific space provided on the Contract Note to affix the stamp, and the counterfoil of the Contract Note specifically provides for the client to acknowledge the Contract Note issued to him and return the counterfoil duly signed, that the requirement of acknowledging the Contract Note is not an empty formality. He submittted that the Respondent vide circular dated 5.8.96 had informed all concerned that failure to maintain counterfoil of Contract Notes with adequate details would be viewed seriously, that the acknowledgement of receipt of Contract Note by the clients is an essential record, as it enables to ensure issuance of Contract Note by the brokers. He further submitted that in terms of rule 15(2) (b) of the Securities Contract (Regulation) Rules, 1957 every broker is required to maintain counterfoil or duplicate of Contract Notes issued to clients. Shri Barua submitted that the Appellant has

not viewed seriously the matter is evident from its reply. He submitted that failure to afffix stamp on the Contract Note is also a violation, in as much as the requirement of affixing the stamp is a requirement as per the Contract Note devised under the regulations, that the Respondent vide its circular dated 29.12.93 had also required all concerned to comply with the said requirement, further that it is also a statutory requirement under the Stamp Act that the Contract Notes bear stamps of adequate value. Learned representative submitted that the Appellant has admitted that in some cases stamps have not been afixed, that failure is in violation of the requirements of the regulation and the directions conveyed in this regard by the Respondent in its circular dated 29.10.1993, that it is also to be noted that the stock brokers were forewarned by the said circular, that failure to affix stamp on the Contract Notes by the broker would be viewed seriously, that despite such a clear warning the Appellant did not comply with the said requirement. He submitted that a stock broker vide clause B(2) of the Code of Conduct forming part of the Stock Broker Regulation is required to issue Contract Note to the client in the form specified by the stock exchange. He submitted that the Appellant's submission that the NEAT System provided for recording of the time when orders were placed and as such the electornic data so retrieved is sufficient is not tenable, that the Respondent has specifically required vide its circular dated 11.2.97, that every stock broker maintain record of the time of placing the order by the client with the broker and record the same on the Contract Note alongwith the time of execution of the orders as the transaction price is relatable to the time factor. In this context he referred to clause B(1) of the Code of Conduct that:

"B. **Duty to the Investor**

(1) *Execution of Orders:* A stock-broker, in his dealings with the clients and the general investing public, shall faithfully execute the orders for buying and selling of securities at the best available market price and not refuse to deal with a Small Investor merely on the ground of the volume of business involved. A stock-broker shall promptly inform his client about the execution or non-execution of an order, and make prompt payment in respect of securities sold and arrangement for prompt delivery of securities purchased by clients.

(2) *Issue of Contract Note*: A stock-broker shall issue without delay to his client a contract note for all transactions <u>in the form specified by the stock exchange."</u> (emphasis supplied)

Shri Barura submitted that client registration form is devised to obtain certain useful information to enable stock broker to know the details/credibility of the client before dealing with him, that client identification is important since that makes it easier for the audit trail to identify the clients, that the details like PAN number, introduction etc. would help to know the credentials of the clients, that not filling up of the client registration forms properly with the details, is in contravention of the Respondent's circulars dated 18.11.1993, 11.2.1997 and 11.4.1997. He submitted that there is only limited scope of relaxation of the input requirements in the form and there is little discretion available to the broker. In this context he referred to circular dated 11.4.97.

Learned representative submitted that as per the circular dated 31.3.1997 no broker shall deal with a person who is acting as a sub broker unless he is regisered with the Respondent. He submitted that the Appellant's contention that the circular dated 31.3.1997 was not circulated by NSE and hence it was not aware of the same is not tenable, that there is no reason to believe that NSE which promptly publishes the Respondent's circulars had chosen not to publish the circular dated 31.3.1997, that in any case the said circular was available on the Respondent's website and the same was issued pursuant to the decision arrived at in the annual meeting of all the stock exchanges, which was made public.

It was submitted that the enquiry officer had listed several instances of off the market transactions by the Appellant, contrary to the Respondent's circular dated 14.9.1999, that as per the said circular it was required that all negotiated deals be executed only on the screen of the exchanges like any other normal trade. Learned representative submitted that the Appellant was found to have carried on off the market transactions to the tune of Rs.15 lakhs during the sample period subjected to inspection. He submitted that off the market transactions are against the transparent transaction requirement and the broker indulging in such transactions deserves to be punished, that the submission of the Appellant that

the violations are of technical nature with no adverse effect on the investors and the securities market is not tenable. Shri Barua submitted that as a condition for grant of the certificate of registration in terms of rule 4 (b) of the SEBI (Stock Brokers and Sub-Brokers) Rules, 1992, every stock broker is under obligation to comply with the statutory requirement prescribed under said regulation, that under section 11 of the SEBI Act, the Respondent is empowered to take measures to protect the interests of investors and to regulate the securities market inter alia by registering and regulating the working of the stock brokers, that the directives contained in the SEBI circulars are measures for regulating the working of stock brokers, that the code of conduct specified in Schedule II also provides for the minimum standards for the working of the stock brokers. If the regulatory requirements are violated by the stock brokers on the ground that the violations are technical and hence not punishable, the measures taken by SEBI for regulation of the stock brokers would be rendered nugatory and the regulatory function would be jeopardized. The requirements of Contract Notes, time stamping etc are the requirements which SEBI has put in place for the purpose of investor protection and to remove certain mala fide practices, and non compliance of SEBI directives cannot be viewed as technical. He further submitted that indulging in transactions which are prohibited can not be allowed on the ground of any technicality or otherwise especially when such transactions are likely to have a detrimental effect on regulation of the securities market, that every stock broker is under obligation to comply with the provisions of the Act and the Rules and Regulations made there under as also the circulars and guidelines issued by the Board from time to time, and that it is also imperative that all the members of the stock Exchange adhere to the bye-laws of the Exchange. It was submitted that Regulation 7 provides that the stock broker holding the certificate shall at all times abide by the Code of Conduct as specified in Schedule II, that Clause A(5) of Schedule II provides that a stock broker shall abide by all provisions of the Act and the Rules Regulations issued by the Government, the Board and the Stock Exchange from time to time as may be applicable to him. According to the Respondent the Appellant has committed several violations as observed in the order and has not taken due care and diligence in observance and compliance of the statutory requirement in conduct of its business as a stock broker, that the Appellant has violated the condition of registration specified in rule 4(b) of the SEBI (Stock Brokers and Sub-brokers) Rules, 1992.

Shri Barua submitted that the ratio in the cases cited by the Appellant has no application to the facts of the case, that the Appellant has admitted the violation, that it was aware of the regulatory provisions and the regulator's instructions, but decided to not to comply with the same deliberately viewing the same as not very important, that in the light of the facts and ciricumstances of the case, suspension of the certificate of registration for six months is in no way harsh or unjustified.

I have very carefully considered the rival contentions and the material on record.

The Appellant is a member of NSE. The Respondent has granted a certificate of registration to the Appellant to act as a stock broker, that it has also been registered under the Futures and Option Scheme as a trading member since 2.6.2000 and as a self clearing Member since 5th July 2002. The Appellant had submitted that vide the impugned order its certificate of registration No.1NB 230776935 was suspended, that as per the letter dated 27.3.2003 forwarding the impugned order the Appellant was informed that it will cease to carry on any activity as an intermediary during the period of the suspension. The Appellant's counsel had submitted that by the said forwarding letter the reach and scope of the order has been stretched. I do not see any scope for any doubt in this regard. A forwarding letter canot supplement a statutory order. The scope and reach of the order is determined with reference to the order proper. In any case, there is nothing on record to show that the Appellant is

also functioning as another intermediary. It has stated in its memorandum of appeal that it was holding "Portfolio Management Licence also for the period 16th March 1995 to March, 2001" under a different registration. Accordingly the validity of the certificate is over by now, in case it has not been renewed. The appellant has not stated that the said registration has been renewed.

On a perusal of the show cause notice issued to the Appellant by the Respondent based on the enquiry report, it is seen that it was held against the Appellant that it had not maintained "Margin Deposit Book" as required vide regulation 17(1)(k) of the Stock Broker Regulations. The Appellant's version is that since it had not collected margin it was not required to maintain the book, and as far as margin deposit made by it with stock exchange, there is a facility of Electronic Down Load and a separate file is being maintained for such margin down load by the Appellant. As the Appellant rightly pointed out that it is not the charge that the Appellant had traded without collecting margin. Hence, the Appelant cannot be penalised in the proceedings initiated by the Respondent viewing that the Appellant traded without obtaining adequate margin. Therefore, the circular dated 18.11.1993 requiring the brokers to collect requisite margin has no application to the instant charge. The Respondent has not controverted the Appellant's contention that it had not collected margin from its clients. In my view the margin deposit book required to be maintained under regulation 17(1)(k) is not only confined to margins received from the clients, but it also covers the margin deposit made by the broker with the exchange. Since the Appellant has claimed that it has not received margin from the clients, the question of furnishing the details of the same in the book do not arise. However, since the Appellant has deposited margin money with the exchange, it was required to be recorded in the margin deposit book. In this connection it is to be noted that the details of the margin deposit are available on the exchanges' computer and available at a click. According to the Appellant, it had down loaded the statement and kept in a file the details in seriatim. This has not been disputed by the Respondent. The Respondent's grievance is not that the material information is not available, its objection is more on the manner in which it is stored. No doubt the ideal thing would have been to literally comply with the requirement of regulation 17((1)(k) to the extent it was applicable to the Appellant. However, since the Appellant is stated to have maintained effectively the record of its margin deposit with the exchange, the failure to maintain the information in the "book form" can not be considered as a grave violation of the regulation to warrant penalty of suspension of its certificate of registration.

In terms of rule 15(2) of the Securities Contract Regulation (Regulation) Rules, 1957 every stock broker is required to maintain and preserve "counter foils or duplicates of contract notes issued to clients". According to NSE Regulation 3.5.1 (Part A) "Every Trading Member shall issue a Contract Note to his constitutents for trades executed in such form as specified in Annexure 2 with all relevant details as required therein to be filled in and issued in such a manner and within such time as prescribed by the Exchange".

I have perused the copy of the format of the Contract Note referred to in the regulation as filed by the Appellant. It is seen from the said format that there is a provision for the client to acknowledge the receipt of the Contract Note by affixing his signature and the counterfoil so signed is required to be returned to the broker. The requirement is either to have the counterfoils or the duplicates of the Contract Notes issued to the clients. This is a very important requirement as it goes to establaish that the Contract Note was actually issued to the client. Contract Note is a very important document in the transaction and its relevance is all the more when dispute arises between the broker and the client. The requirement of affixing the stamp on Contract Note is a requirement under the Indian Stamp Act

independent of the Stock Broker Regulations or Regulations of Exchanges. If stamps of adequate value are not affixed, the consequences as provided under the Stamp Act will follow. But at the same time it is for the broker to ensure that the stamps of adequate value are affixed on the contract note. The duty is cast upon him. It is noted that the Appellant has admitted its failure in this regard. The Contract Note provides space for recording "Trade time". This "Trade time" is the one which refers to execution of the trade. Not the placement of the order by the client. However, according to the Respondent, its ciricular dated 11.2.97 requires every stock broker to maintain record of time of placing the order with it. According to the said circular (it is addressed to the Stock exchanges) "the broker member should maintain record of time when the client has placed the order and reflect the same in contract note along with the time of execution of the orders". By the said circular the stock exchanges were directed to initiate action in this regard. The Appellant's submission that NSE had not circulated the said circular is not convincing. Failure to carry out the Respondent's direction by NSE would have attracted consequences. In any case the said circular was displayed on the Respondent's Website. The receipt of the order from the client and execution of order by broker are not one and the same. Stamping the receipt time is important from the investor protection angle as it has a bearing on the transaction rate. Failure to do so is a matter of concern. It is noted from the NSE Regulation (6.1.3) that a stock broker is required to maintain order book reflecting therein amongst other details, the date and time of orders received from clients. Therefore it is not that there is no other source to locate order receipt time, in the event of any dispute. But this information is not readily available to the client. The Appellant's argument that the format of the Contract Note was not amended and therefore it was not required to do time stamping has no basis. It is well settled that an administrative circular is effective as an interim measure till the regulations are amended incorporating the requirement of the circular. In my view the Respondent's charge of the default on the part of the Appellant in complying with the requirements of retaining counterfoil/duplicate of the contract note, stamping time of receipt of the order and affixing stamps, as per the Indian Stamp Act stand established.

The deficiencies in few client registration forms, that one of such forms did not provide identity of the client, that in another photo and proof of identify/residence was missing and in 3 other cases Annual Income and Income Tax PAN number were not found, in my view are not serious lapses so as to invoke penal action. The client registration form is not a document of guarantee. It provides certain inputs. If there are supplementary information to satisfy the credentials of the client, few insignificant omissions in the matter is not fatal. In any case the Appellant has stated that it has made good those deficiencies.

The Appellant has not denied the charge that it had carried out off the market transactions and the same has not been reported to NSE as required vide circular dated 14.9.1999. The Apellant's argument that the amount involved was only Rs.15.07 lakhs as against the Appellant's annual turnover of Rs.1987 crores in 1999-2000, and Rs.1780 crores in 2000-2001, does not absolve it of the charge. Violation is not relatable to the size of the transactions. Violation is with reference to the compliance requirements. The enquiry officer has stated that the Appellant had admitted that these transactions are off the market transactions. According to the Appellant these transactions were done when the share prices had reached circuit filter limit and there was no way a client could execute transaction at this level. It is noted that SEBI vide its circular dated 1.9.1999 had prohibitted all negotiated and off market deals since it considered the same not transparent and not helpful to price discovery process on the stock exchange mechanism. The fact of making off the market transaction – though the amount involved is only Rs.15 lakhs – has been admitted by the Appellant. The action of the Appellant is in violation of the Respondent's circular dated 1.9.1999. The Appellant's argument that the said circular

has no binding force is not tenable. The Respondent is mandated to protect the interest of the investors in securities and the securities market by taking suitable measures. The circular dated 1.9.1999 is in pursuance of the said mandate and therefore binding on all those concerned.

The Respondent has viewed that the Appellant had carried out transactions with members of Calcutta Stock Exchange who were neither registered as remisiers with NSE nor were they regisered as sub brokers with the Respondent, in violation of the Respondent's circular dated 31.3.1997. The entities with whom the Appellant had traded are stated to be Kamani Stock Broking and four others. The Appellant has not denied having traded with the said entities. But its contention is that they are not sub brokers. According to the Appellant the Kamani Stock Broking was trading with the Appellant on its own and not for its clients, that the requirement regarding registration as sub broker or aprpoval as remisiers is relevant only when they are working for their clients and not for themselves, that the Appellant traded with them as clients and traded in their name only, that there was no information with the Appellant to believe that they are sub brokers, that the bill, Contract Notes, Cheques etc. were issued in their name.

I do not find any supporting evidence in the impugned order to establish that the said entities were acting as sub brokers/remisiers. There is no prohibition on trading on NSE for a broker of another exchange. The evidence on record shows that the Appellant was trading for them as a client proper and not as a sub broker. Dealing with unregistered broker is in violation of the Regulations. But then the charge has to be reasonably proved. Size of the transaction by itself is not the clincher. The evidence is required to show that the client was acting as a sub broker. The Appellant's argument that it was not aware of the Respondent's circular in this regard is of not much relevance in the light of paucity of evidence from the Respondent to substantiate the charge. In the absence of reasonable evidence it is not possible to subscribe to the Respondent's version holding the Appellant guilty of trading with unregistered sub brokers/unapproved remisiers.

The learned Counsel for the Appellant had submitted that Respondent has simply attempted to match the failure with circulars/regulations and totally ignoring the effect of such failure imposed penalty which is disproporationate to the gravity of the charge. He had also alleged that the Respondent had ignored the factors to be noted for the purpose of imposing penalty as provided in Section 15J of the Act.

It is to be noted that the Appellant's reliance on section 15J is of no help as the said section is applicable to the adjudicating officer imposing monetary penalty. The parameters for deciding suspension/cancellation of the certificate of registrtion of a broker is broadly provided in the Stock Broker Regulation itself. I do not find that the decision in Hindustan Steel, Escort, Cabbott, LKP etc. relied on by the Appellant is of any help to estabalish that the penalty imposed is unwarranted, in the light of the facts and circumstances of the instant case as discussed above.

It is well settled that the nature and quantum of penalty should be proportionate to the gravity of the offence committed. In the light of the finding recorded above, I am of the view that the penalty of suspension of the certificate of registration of the Appellant for six months is certainly disproportionate to the charges proved. Suspension of the certifificate of registration of an intermediary, as observed by

the Tribunal in MJ Patel (supra) is a serious matter. Some of the charges levelled against the Appellant have failed and some of the charges have been established. I have considered the nature of the penalty imposed in the light of the above findings. In the light of the facts and circumstances of the case, I do not find adequate justification to suspend the certificate of registration for a period of six months and thereby put the Appellant out of business for such a long period. But at the same time, I find that the Appellant had failed to comply with certain requirements such as proper recording of certain matters in the Contract Note, not reporting the off the market transaction etc. discussed in detail above. These failures are not that trivial to be condoned. The fact that there were no complaints against the Appellant does not absolve it from the legal consequences for its omissions and commissions as a stock broker. Taking into consideration all the relevant aspects I am of the view that suspending the certificate of registration for a period of two months would be in commensurate with the failure/omissions/commissions by the Appellant. Accordingly that part of the impugned order suspending the certificate of registration for a period of six months is modified by reducing the suspension period to two months. The rest of the order to be sustained. The suspension of the certificate of registration will come into effect after three weeks from today.

The order as modified, is upheld.

The appeal disposed of in the above lines.

Sd/-

(C. ACHUTHAN)

PRESIDING OFFICER.

Place: Mumbai

Date: May 30 , 2003.