

**In Re: Inspection of Depository**

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**SooperKanoon Citation :** [sooperkanoon.com/58423](http://sooperkanoon.com/58423)

**Court :** SEBI Securities and Exchange Board of India or Securities Appellate Tribunal SAT

**Decided On :** Aug-22-2006

**Judge :** V Chopra

**Appellant :** In Re: Inspection of Depository

**Judgement :**

1. Infrastructure Leasing & Financial Services Limited (hereinafter referred to as IL&FS) is a corporate body engaged in business of leasing, infrastructure and project and Investment Banking. IL&FS is a depository participant of National Securities Depository Limited (NSDL) and Central Depository Services Limited (CDSL) and registered with Securities and Exchange Board of India (hereinafter referred to as SEBI) under Certificates of Registration Nos. IN-DP-NSDL-02096 & IN-DP-CDSL-52-2000.

2. Inspection of books of accounts, records, documents etc of the depository participant activities of IL&FS was undertaken by a SEBI appointed CA firm, M/s. Khimji Kunverji & Co. for the period starting from its inception till 31st October 2002. The inspection at IL&FS was undertaken as Depository Participant of NSDL. Certain irregularities, deficiencies and lapses on the part of IL&FS were observed by the said CA firm. Same were communicated to IL&FS vide letter dated January 27, 2003 and it was given 15 days time to offer its comments on the observations of inspection. IL&FS vide its letter dated March 10, 2003 furnished its reply to the said observations.

3. After considering the submissions made by IL&FS, a show cause notice was issued to it on May 6, 2004, advising it to show cause as to why cease and desist proceedings under Section 11D of SEBI Act, 1992, should not be initiated against it for the lapses and irregularities observed during the inspection. The following allegations were made in the show cause notice against IL&FS: a) Beneficiary accounts were opened without obtaining proper proof of identity and address of the clients, thereby violating the provisions of SEBI circular No. SMDRP/Policy/CIR-36/2000 dated August 04, 2000.

b) Beneficiary accounts were opened with improper and incomplete documentation like, absence of certificate of incorporation, absence of signature of witness, accepting documents without verification with the originals and incomplete nomination form.

d) Delayed closure of the beneficiary account and charging the investor till the closure of the account.

e) Instances of not mentioning or mentioning incorrect ISIN on the demat request form (DRF), mentioning extra account holders in DRF and not mentioning the beneficiary ID on the DRF resulting in the delay of dematerialisation and rejection by the registrar or the issuer company.

f) Instances of accepting DIS without time-stamping, without date of acceptance, non-mention of ISIN on the Demat Instruction Slip (DIS), difference in the execution date and actual execution, and difference in the quantity as mentioned in the DIS and as showing in the system.

g) Investor complaints were not recorded, complaints register was not being maintained and correspondence pertaining to the same was being filed only after June 2000. Even after starting to maintain the records the date and time of receipt of grievances was not generally recorded on the grievance and in its absence whether the redressal of grievance was within 30 days cannot be found out in terms of Regulation 20(2) (e) of Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996.

4. IL&FS was advised to send its reply to the said show cause and also indicate if it desired a personal hearing before the competent authority. A reply to the show cause notice was received from IL&FS vide letter dated June 07 2004. IL&FS, in its reply, while replying pointwise to the show cause notice admitted that there were certain short comings and compliances to be fulfilled in specific areas, but stated that these lacunae were not rampant. IL&FS sought for an opportunity for a personal hearing.

5. An opportunity of personal hearing was given to IL&FS on July 21, 2006. IL&FS appeared on the said date through the officials as mentioned in the first page of this order and made submissions reiterating its written reply. Further, IL&FS filed written submissions dated 24.7.06.

6. I have carefully considered the inspection report, the show cause notice, the reply of IL&FS and the material available on record and my findings are as follows.

6.1 With regard to the allegation that IL&FS had opened beneficiary accounts without obtaining proper identity proof of the client, without obtaining address proof and had thereby violated the provisions of SEBI circular No. SMDRP/Policy/Cir-36/2000 dated 04.08.2000, IL&FS contended that they had introduced check list approach to safeguard interests of the investors. It also enclosed a copy of the checklist for immediate reference and stated that the same is scrupulously followed. IL&FS assured that all these documentations were proper ensuring safe, secured and efficient functioning of the depository system.

6.2 With regard to the allegation that the DP had opened beneficiary accounts with improper and incomplete documentation like absence of signature of witness, accepted documents without verification with originals etc., IL&FS submitted that they exercised proper care and have taken effective steps towards observing due diligence in completion of legal procedures, as set out in the system.

6.3 From the above submissions, I find that the DP did not deny the violation alleged against them. Opening of beneficiary account by following incomplete procedure will result in misuse of depository system. However many of the violations found out by the Inspection team pertains to the period before the issue

of the circular dt 04.08.2000.

6.4 With respect to the charging of Beneficiary account holders even after the receipt of application to close the Accounts, IL&FS submitted there were some delay in closing the Accounts due to completion of procedural formalities. IL&FS submitted that it charged the Account holders only upto the period of receipt of the application forms for closure.

6.5 With respect to the instances of IL&FS having not mentioned ISIN on the demat request form (DRF), mentioned incorrect ISIN on the DRF ,mentioning extra account holders in DRF and non mentioning of the beneficiary ID on the DRF resulting in the delay of dematerialisation by the registrar or the issuer company IL&FS admitted instances of 14 cases and submitted overall process have been reviewed and strengthened.

6.6 With respect to the Instances not placing of time stamping, non mentioning date of acceptance, non mentioning of the ISIN on the DIS, difference in the execution date as mentioned on the DIS, difference in actual execution, difference in the quantity as mentioned in the DRF and as shown in the system, IL&FS submitted that the instances are few.

6.7 With regard to the allegation that complaints were not recorded, complaints register was not being maintained and that correspondence pertaining to the same was being filed only from June 2000 onwards, IL&FS stated that although they did not have structured maintenance of systematic book, all the complaints were attended to in all seriousness. I find the number of instances cited are lesser in number.

Regulation 20(2)(e) of SEBI (Depositories Participants) Regulations, 1996 mandates the depository participant to redress the grievances of beneficial owners within 30 days of the date of the receipt of the complaint and keep the depository informed about the number and the nature of redressal. For complying with the above said regulations and having an effective redressal mechanism, it is necessary for the participant to have and maintain proper books, records and filings of the complaints and correspondence pertaining to the same. I find that

IL&FS had admitted that they did not maintain structured and systematic books regarding complaints.

6.8 Upon considering all the facts of the case, I agree with the findings of the inspection report that IL&FS had committed irregularities discussed above, as which are violative of the provisions of SEBI circulars SMDRP/Policy/Cir-36/2000 dated August 04, 2000 and Regulation 20 of SEBI (Depositories & Participants) Regulations, 1996. These violations do not augur well for the securities market, as in a demat environment, a DP plays a crucial role and any systemic deviation will expose the investors to avoidable and unforeseen risks, which would not be conducive to the orderly development of the securities market. However I have noted that the irregularities pertain to a period before 2000 and six years have elapsed. IL&FS has stated that the said irregularities have been rectified. In view of this, it would not be appropriate to issue orders or directions at this stage asking IL&FS to cease from committing violations. I have also noted that almost similar violations have been prima facie found as recorded in the ad interim ex-parte order dt.27.04.06 read with order dated 28.7.06 in the case of IPO investigations. I have also noted that an enquiry officer was appointed and the enquiry proceedings are pending.

7. In view of the above, in the interests of investors and to safeguard the integrity of the securities market, in exercise of powers conferred upon me by Section 19 read with Section 11D of the Securities and Exchange Board of India Act, 1992, I hereby direct Infrastructure Leasing and Financial Services Limited to desist from repeating any of the aforesaid lapses. Any repetition of such violations would be viewed seriously and invite penal proceedings.

8. This order shall come into force with immediate effect. It is also clarified that this order shall be without prejudice to any other proceedings pending before SEBI against IL&FS.

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