

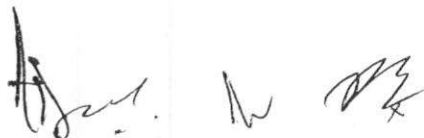
MCX STOCK EXCHANGE LTD.
DISCIPLINARY ACTION COMMITTEE
ORDER UNDER RULES 1 & 2 OF THE RULES OF MCX STOCK EXCHANGE LIMITED

1. Background

- 1.1. Composite Securities Ltd (CSL or the "Member") (Member ID 13200) is a Trading Member on the Currency Derivatives (CD) segment of MCX Stock Exchange Ltd. ("the Exchange") and is registered with Securities and Exchange Board of India (SEBI) as a trading member on CD segment of the Exchange with registration No. INE260775437 dated September 25, 2008.
- 1.2. A regular inspection of CSL covering the period April 01, 2011 to March 31, 2012 was conducted by the Exchange in May 2012.

2. Inspection Finding – Transfer of Trades in the Back-office of the Member

- 2.1. During the inspection, it was observed that the member had executed trades in the account code of one Mr. Sandeep Handa, his client (Client Code – 2762), and had subsequently transferred some of the said trades to its own 'error' account in the back office after the trading hours.
- 2.2. The member had executed a sell order for 1000 contracts of EURINR and a buy order of 900 Contracts of EURINR on August 18, 2011 in the above-mentioned client code. Out of this, it was found that he had transferred executed trades for buy and sell of 900 contracts each to his error account in the back office. The 900 contracts were acquired and later squared off through a total of 132 trades on same date, which were then transferred to 'error' account.
- 2.3. The member incurred a loss of Rs. 63,204/- while squaring off the transactions and the said loss was also transferred by the member to his 'error' account. The value of trades transferred amounts to Rs. 11,87,20,830/- the percentage of trades transferred during the month of August, 2011 was 65.32%.
- 2.4. The member retained sell orders of 100 Contracts of EURINR in the client account and issued a contract note to the client for the said 100 contracts.
- 2.5. The member's explanation for the above when confronted with the inspection observations as above was that the trader had put in an order for 1000 contracts erroneously instead of 100 contracts required by the client. Upon realizing the mistake, the excess 900 contracts were immediately squared off and the trades resulting in booking of 900 contracts and their subsequent square-off were transferred offline at end of the day to the member's 'error' account, to rectify the mistake. The correct 100 contracts were retained with the client.



- 2.6. An initial observation letter dated May 28, 2012 was sent to the member, seeking comments / clarifications on the non-compliances observed during inspection, which was responded by CSL vide his letter dated June 18, 2012. CSL had mentioned regarding the transfer of trades issue in their reply that the incident was a wrong execution caused due to punching error and that the transaction was transferred to their account to avoid problems in calculating the loss which would have involved charges such as service tax, brokerage etc. CSL submitted that they had transferred the loss of about Rs. 63,000/- to their account.

3. Member's Explanation on transfer of trades:

- 3.1. The Member submitted its reply to the observation letter, by its letter dated June 18, 2012 and an email dated December 7, 2012. A summary of the Member's reply is as under:

- i. They have adhered to the Exchange Circular No. MCX-SX/ID/629/2011 dated August 26, 2011
- ii. The loss of Rs. 63,204/- was transferred to their own 'error' account
- iii. This particular transaction took place between the intervening period of issue of SEBI circular dated July 5, 2011 and defining genuine error and guidelines by the Exchange on August 26, 2011
- iv. This cannot be taken as modification of trades

4. Disciplinary Action Proceedings:

4.1. Hearing Notice

Vide notice no. MCX-SX/INSP/116/2012/14925 dated December 03, 2012, the Exchange granted personal hearing to the member before the DAC on December 18, 2012.

4.2. Personal Hearing before the Disciplinary Action Committee

CSL was granted an opportunity of hearing before the Disciplinary Action Committee of the Exchange on December 18, 2012. Mr. Sanjeev Dhupar, the Designated Director of CSL, appeared in person before the Committee. He made the following submissions during the hearings:

- (a) This incident was purely a mistake of the dealer. The mistake was corrected as soon as it was noticed.
- (b) At the relevant point of time, there was no clarification as to how such error was to be handled. The clarification given by the Exchange was issued subsequently.
- (c) From the very nature of the transaction it can be made out that it was a genuine error. The mistake was realized within 7 minutes and immediate corrective action was taken to reverse the trades.
- (d) CSL's past record was very clean and they had not modified any other trade before.
- (e) On a query by a DAC member, he mentioned that the transfer was not done online as there was no process in place for such online transfer at that point in time, as the Exchange clarification had come in later.
- (f) CSL had got a confirmation from the client also regarding the transaction.



(g) The parameter for judging a member's conduct should not be individual transactions but rather a holistic view should be taken.

(h) Having regard to the above and having regard to the fact that CSL had already suffered a loss of Rs. 63,000/- due to the error, the penalty may be reduced to the maximum extent possible, if penalty is inevitable.

5. CONSIDERATION OF ISSUES

- 5.1. We have carefully considered the material on record including the replies filed and submissions made by CSL.
- 5.2. It is apparent from the factual matrix that the transfer of trade was done to correct an error, as contended by CSL. The excess trades of 900 contracts was reversed by CSL in the client's name itself and thereafter transferred to its error account at the end of the day offline.
- 5.3. We tend to agree with CSL that as on the date of occurrence, i.e., on August 18, 2011, there was no framework or clarification from exchanges on how to deal with such an error. The uniform clarification was issued by MCX-SX and other exchanges on August 26, 2011 laying down what constitutes 'genuine error' and the procedure for transfer of erroneous trades to error account. In terms of the said clarification, CSL ought to have transferred the trades to the error account online and thereafter liquidated or closed out. Instead they had reversed the trades from the same client's account and thereafter transferred both the original and reversal trades to their error account and absorbed the loss. The explanation for this deviation is that the clarification was not issued by the date of the transaction and they had done the best that they could under the circumstances to rectify the error. We tend to agree with this explanation.
- 5.4. The regulatory requirements relating to transfer of trade/ Modification of Client Codes of Non-Institutional Trades have undergone a significant change with the issue of SEBI Circular dated July 05, 2011, which has been effective from August 1, 2011, whereby stringent and uniform penalty across exchanges was introduced. Pursuant to Joint Meeting of Exchanges with SEBI, all the Exchanges had issued clarification on August 26, 2011 clarifying inter alia as to what would constitute genuine error and the procedure to rectify the same. In light of the above discussion, CSL had substantially complied with the procedure for error account transfer and could not be taken to have violated the above circular.
- 5.5. We note that the Exchange levies penalty on back office transfer of trades @ 0.1% of values of trades transferred, if instances of such transfer are in excess of 2% of numbers of orders executed. The relevant extract of Exchange Circular no. MCX-SX/INSP/528/2011 dated March 1, 2011 which provided for the same at the relevant point of time, is reproduced below:

Transfer of trades / Errors at the time of order entry	If instances in violation are in excess of 2% of number of orders executed, fine of 0.1%
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- 5.6. Although erroneous in nature, the said transfer of trades fall within the prohibition of the above circular. An offline transfer of trade is prejudicial to market integrity, as the Exchange would have no record of the same having been undertaken, but for the inspection. In records of the Exchange, which may be shared with other regulatory and statutory authorities, the original client would appear as the party who undertook the transactions. Hence, it would be in order to impose the penalty as required by the Exchange Circular dated March 1, 2011.
- 5.7. If the above scale is applied, the number of instances transferred to error account amount to 48% of number of orders executed during the month of August 2011. Applicable penalties, if calculated as per the above penalty structure for the Member would then 0.1% of the traded value, which was Rs. 11,87,20,830/-, i.e., a penalty of Rs. 1,18,721/-. Having regard to the fact that the trades were erroneous and were subsequently reversed, and taking into consideration the submissions of the member, we feel that only 50% of the transfers should be attributed to violations in terms of this circular. Accordingly, the ends of justice would be met if the penalty is levied only on one side of transaction i.e., on approximately 50% of the total traded value i.e., if penalty of Rs. 59,360/- is charged.
- 5.8. We further note that CSL has absorbed the loss occasioned in this entire episode, which amounts to Rs. 63,204/-, which also persuades us to reach the above conclusion.
6. **DIRECTIONS**
- 6.1. In view of the above, and in terms of Exchange circular no. MCX-SX/INSP/528/2011 dated March 01, 2011 we hereby impose a penalty of Rs. 59,360/- on CSL. The same should be paid to the Exchange within 60 days of date of receipt of this order.

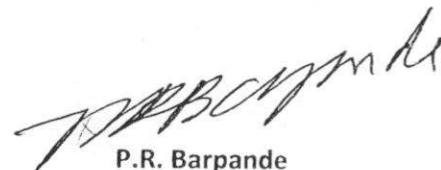
Dated on 21st day of March, 2013.



Asha Das



Joseph Massey



P.R. Barpande

CERTIFIED TRUE COPY

For MCX-Stock Exchange Ltd.



Company Secretary