

**Member and Core Settlement Guarantee Fund Committee
("MCSGFC"/"Committee")
of
National Stock Exchange of India Limited
Exchange Plaza, Bandra-Kurla Complex, Bandra East, Mumbai – 400051
held on February 16, 2023**

In the matter of the Trading Member M/s. FNO India Securities Private Limited

CORAM:

Ms Mona Bhide	- Chairperson
Mr K Narasimha Murthy	- Committee Member
Mr S Ravindran	- Committee Member
Mr Ranganayakulu Jagarlamudi	- Committee Member
Mr Ashishkumar Chauhan	- Committee Member

ALSO PRESENT:

Ms Priya Subbaraman	- Chief Regulatory Officer
Dr Dinesh Kumar Soni	- Senior Vice President - Regulatory
Mr Shailesh Adukia	- Vice President - Regulatory

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1. **M/s. FNO India Securities Private Limited ("Noticee")** is a Trading Member registered with the National Stock Exchange of India Limited ("**Exchange**"/"**NSEIL**") and enabled for trading in the Capital Market ("**CM**") and Futures & Options ("**F&O**") segments since July 2019 and Currency Derivatives ("**CD**") segment since May 2019.
 2. The Exchange conducted a limited purpose inspection of the Noticee's books and records covering the period January 2021 to June 2022, across segments, from September 2022 to November 2022. Post-inspection, the Exchange issued a show-cause notice dated January 3, 2023 ("**SCN**") to the Noticee to seek an explanation for the observed non-compliances with the regulatory provisions. The Noticee vide its letters dated January 13, 2023, and February 17, 2023, replied to the SCN.
 3. The Exchange observed several non-compliances during the inspection. However, at this stage, in the interest of the investors and integrity of the

securities market, the Committee deems fit to pass interim directions for the non-compliances pertaining to falsification of client registration documents and unique client code data without going into the merits of other non-compliances mentioned in the SCN which shall be dealt subsequently by a separate order.

4. Before dealing with the non-compliances, it would be appropriate to refer to the relevant regulatory provisions which are alleged to have been violated by the Noticee. The relevant extracts thereof are reproduced hereunder:

4.1 **Falsification of client registration documents**

- a. Exchange Circular No. NSE/INVG/2007/9424 dated August 31, 2017

Customer Due Diligence/KYC Standards

New customer acceptance procedures, inter alia, could include processes:

- a) ...
- b) ...
- c) *For clearly establishing identity of the client, verification of addresses, phone numbers and other details.*
- d) ...
- e) *For verifying the genuineness of the PAN provided by the client such as comparing with original PAN, checking details on the Income tax website etc.*
- f) *To check original documents before accepting a copy.*
- g) *Apart from the mandatory information specified by SEBI, members should ask for any additional information as deemed fit on case-to-case basis to satisfy themselves about the genuineness and financial standing of the client.*
- h) ...
- i) ...
- j) ...

k) ...

l) *Risk based KYC procedures should be adopted for all new clients.*

m) *The information obtained through the above-mentioned measures should be adequate enough to satisfy competent authorities (regulatory / enforcement authorities) in future that due diligence was observed by the intermediary in compliance with the Guidelines.*

b. Rule 2 of Chapter IV of NSEIL Rules

Penalty for Misconduct, Unbusinesslike Conduct and Unprofessional Conduct

(2) *In particular and without in any way limiting or prejudicing the generality of the provisions in Rule (1) above, a trading member shall be liable to expulsion or suspension or withdrawal of all or any of its membership rights and/or to payment of a fine and/or to be censured, reprimanded or warned for any misconduct, unbusinesslike conduct or unprofessional conduct in the sense of the provision in that behalf contained herein.*

4.2 Observations pertaining to UCC data

Exchange Circular No. NSE/INVG/21841 dated October 4, 2012

All Trading Members are requested to review the details of the clients uploaded on UCI Online pertaining to their mobile number and / or email address and update the same wherever necessary.

Trading Members are hereby requested to take utmost care while uploading client details including mobile number and email address on UCI - ONLINE.

PRESENT MCSGFC PROCEEDINGS

5. The Exchange, vide its email dated February 10, 2023, granted the Noticee with an opportunity for a personal hearing before the Committee. On behalf of the Noticee, Mr. Thomas Joseph – Director & Compliance Officer and Mr. Sanyam Aggarwal – Authorized Representative, attended the personal hearing and submitted as under: -

- a. The Noticee started its operations at the end of 2019. The creation of non-compliant accounts pertains to the COVID-19 pandemic period when the Noticee was offering referral schemes.
- b. The clients appears to have edited the photo images on the PAN and Aadhar and submitted the documents to the Noticee at the time of onboarding. The Noticee verified the name of the clients with their PAN and Aadhar, and the photo at the time of in-person verification.
- c. The Marketwolf application only does options trading with a threshold on profit and loss. All trades are pre-paid.
- d. The Noticee paid approx. Rs.12 to Rs.14 crores towards referral schemes. The brokerage income earned by the Noticee would be in lakhs.
- e. The Noticee has a client base of 7 lakhs. The Noticee took corrective steps to inactivate around 50,000 to 60,000 non-compliant accounts in and around August 2022. In the case of many clients, there were no transactions executed in their accounts. The Noticee now integrated the Marketwolf application with DigiLocker and KYC Registration Agency (KRA).
- f. The Noticee is not involved in money laundering schemes.
- g. The Noticee is willing to get its systems audited.

OBSERVATIONS/VIOLATIONS & REPLY

6. Falsification of client registration documents

6.1 The Exchange observed the following irregularities:

- a. Appearance of single client in multiple videos for in-person verification (VIPV)

Upon scrutiny of the know your client documents of 100 clients selected for sample scrutiny, the Exchange observed that 9 persons appeared as clients in the case of 47 VIPV as per the table below:

Sr. No.	Count of clients
1	7
2	3
3	9
4	2
5	5
6	8
7	4
8	7
9	2
Total	47

b. Non-adherence to customer due diligence process

Upon scrutiny of the know your client documents of 100 clients selected for sample scrutiny, the Exchange observed that the Noticee failed to adhere to customer due diligence process, viz. client onboarding, as under:

- Photograph of 1 person appeared in the KYC documents of 3 clients (Client Codes: 01AAD23849, 01AAD21138 and 01AAC50035)
- Out of the said 3 clients, the PAN of 1 client (Client Code: 01AAD23849) is invalid as per the Income Tax website. Furthermore, the PAN of the said 3 clients (Client Code: 01AAD23849, 01AAD21138 and 01AAC50035) is created on the same date (as per the date appearing on the PAN cards)
- Aadhar number of 3 clients are invalid as per the UIDAI website
- Partial address of 20 clients is captured in the KYC documents and UCI database

6.2 In reply to the SCN, the Noticee submitted as under:

a. Appearance of single client in multiple videos for in-person verification (VIPV)

A sample size of merely 100 clients is biased and is not reflective of all the accounts opened on the Marketwolf application. The Noticee

provided copies of KYC documents of approx. 25,000 clients including the account opening forms and ancillary supporting documents.

b. Non-adherence to customer due diligence process

A sample size of merely 100 clients is biased and is not reflective of all the accounts opened on the Marketwolf application.

- c. There has been no falsification of any client related documents. The Marketwolf application cannot and does not contain any feature or function for editing or changing either the documents or the contents of such documents submitted by the clients.
- d. Due to COVID-19 pandemic, there was a huge inflow of new users to the trading platform of the Noticee. The KYC records inspected by the Exchange were created during the COVID-19 pandemic period when the entire team worked from home. Due to limited resources during lockdown and work from home mode of working, the Noticee was unable to maintain effective quality control.
- e. The Noticee has a detailed unique audit trail of e-signs and VIPV which clearly indicates that the clients have initiated and e-signed their own KYC documents. The Noticee provided a sample audit trail report to the Exchange.
- f. The Noticee acquired its depository participant license in October 2021. CDSL conducted multiple audits and inspections of the Noticee. CDSL did not find any contravention/adverse observations in the said audits and inspections. The Noticee provided the depository participant license and the latest inspection report from CDSL which specifically pertained to KYC compliances to the Exchange.
- g. The Noticee deactivated all the client accounts mentioned in the observation in August 2022 which is prior to the inspection initiated by the Exchange in September 2022.
- h. The entire KYC process is automated and there is no human intervention. The KYC documents are uploaded and self-authenticated by the clients themselves. The application only collects the clients' documents and stores them. Thus, there is no possibility of falsification of the said documents as the application has no feature to edit the documents received from the clients in any manner.

7. Observations pertaining to UCC data

7.1 Upon verification of the UCC records, the Exchange observed the following:

- a. Single email ID mapped to multiple client accounts: 2,499 email IDs mapped to 10,252 clients
- b. Single mobile number mapped to multiple client accounts: 5 mobile numbers mapped to 10 clients
- c. Inappropriate client category selected in UCI database: 20 clients
- d. Single PAN mapped to multiple clients: 12 PANs mapped to 24 clients
- e. Single bank account number mapped to multiple clients: 3,475 bank account numbers mapped to 25,254 clients
- f. Records of active clients available with the Exchange but not recorded in the Noticee's back office: 74,800
- g. Records of active clients recorded in the Noticee's back office but not available with the Exchange: 45,640 clients
- h. Mismatch in PAN between the Noticee's back-office records and Exchange records: 106 clients
- i. Mismatch in email ID between the Noticee's back-office records and Exchange records: 3 clients
- j. Multiple clients with same date of birth: 515 clients mapped to 9 dates
- k. Multiple clients with same address and bank account: 844 clients mapped to 9 addresses
- l. Multiple clients with similar names, location, bank account number and email ID but different PAN
- m. Clients below 18 years of age who have traded in the derivatives segment (Bank Nifty Option Contract): 14 clients
- n. Clients above 90 years age who have traded in derivatives segment: 13 clients

7.2 In reply to the SCN, the Noticee submitted as under:

- a. Single email ID mapped to multiple client accounts: 2,499 email IDs mapped to 10,252 clients

The issue mainly arose due to a technical glitch in the Marketwolf application of the Noticee. The Noticee, vide its email dated September 11, 2022, provided a root cause analysis of the issues and steps taken for resolution. The Noticee deactivated all the client accounts mapped to a single email address since August 2022 which is prior to the inspection initiated by the Exchange in September 2022.

- b. Single mobile number mapped to multiple client accounts: 5 mobile numbers mapped to 10 clients

The issue mainly arose due to a technical glitch in the Marketwolf application of the Noticee. The Noticee deactivated all the accounts mapped to a single mobile number since August 2022 which is prior to the inspection initiated by the Exchange in September 2022.

- c. Inappropriate client category selected in UCI database: 20 clients

The Noticee deactivated all the accounts with inappropriate client category since August 2022 which is prior to the inspection initiated by the Exchange in September 2022.

- d. Single PAN mapped to multiple clients: 12 PANs mapped to 24 clients

Since 12 clients closed their old accounts and opened new accounts, the number of clients increased to 24. The Noticee deactivated repetitive accounts since August 2022 which is prior to the inspection initiated by the Exchange in September 2022.

- e. Single bank account number mapped to multiple clients: 3,475 bank account numbers mapped to 25,254 clients

The issue mainly arose due to a technical glitch in the Marketwolf application of the Noticee. The Noticee deactivated all the accounts mapped to a single bank account since August 2022 which is prior to the inspection initiated by the Exchange in September 2022.

- f. Records of active clients available with the Exchange but not recorded in the Noticee's back office: 74,800

The Noticee denied the observation since the Noticee has the records of active clients in its back-office. The Noticee provided a file containing such records to the Exchange.

- g. Records of active clients recorded in the Noticee's back office but not available with the Exchange: 45,640 clients

The Noticee denied the observation since the Noticee located these clients in the UCI database of the Exchange. The Noticee provided a file containing such records to the Exchange.

- h. Mismatch in PAN between the Noticee's back-office records and Exchange records: 106 clients

The Noticee is yet to update its database.

- i. Mismatch in email ID between the Noticee's back-office records and Exchange records: 3 clients

The Noticee is yet to update its database.

- j. Multiple clients with same date of birth: 515 clients mapped to 9 dates

The possibility of clients' date of birth clashing with each other cannot be ruled out and the Noticee cannot be held responsible for the observation.

- k. Multiple clients with same address and bank account: 844 clients mapped to 9 addresses

The issue mainly arose due to a technical glitch in the Marketwolf application of the Noticee. The Noticee deactivated most of the accounts mapped to the same address and bank account since August 2022 which is prior to the inspection initiated by the Exchange in September 2022.

- I. Multiple clients with similar names, location, bank account number and email ID but different PAN

The issue mainly arose due to a technical glitch in the Marketwolf application of the Noticee. The Noticee deactivated all such accounts since August 2022 which is prior to the inspection initiated by the Exchange in September 2022.

- m. Clients below 18 years of age who have traded in the derivatives segment (Bank Nifty Option Contract): 14 clients

In April 2022, as soon as it came to its notice, the Noticee deactivated such accounts.

- n. Clients above 90 years age who have traded in derivatives segment: 13 clients

The Noticee stopped on boarding any new clients aged above 90 years.

CONSIDERATION & FINDINGS

8. The Noticee failed to maintain adequate controls to ensure clients' due diligence, viz. client onboarding. Furthermore, the Noticee failed to maintain even the basic checks and controls such as running de-duplication of email ID, mobile number, bank account etc. Though the KYC process is automated via Marketwolf application, the Noticee is required to validate the KYC information with relevant supporting documents to ensure the correctness of the data submitted by the clients. Thus, the Noticee acted negligently in handling client information.
9. While the Noticee admits to the technical glitches in the Marketwolf application, it failed to report to the Exchange. It was only when the Exchange identified the non-compliance during the inspection, the Noticee provided the root cause analysis of the issues to the Exchange in September 2022. The root cause analysis is undated and uncertified and therefore its authenticity cannot be ascertained. It is the responsibility of the Noticee to put in place a framework to deal with technical glitches and report such technical glitches to the Exchange immediately.

10. The Noticee failed to have adequate capacity planning to deal with the inflow of new users to the trading platform of the Noticee. The Noticee is solely responsible for such acts of negligence and omission in onboarding the clients without verification thereby posing a systemic risk.

11. The Noticee failed to deploy adequate monitoring mechanisms within the Marketwolf application to generate timely alerts. Furthermore, it is imperative for the Noticee to rigorously test the Marketwolf application before it is made available to the investors.

DECISION

12. In view of the foregoing, the Committee opines that urgent steps need to be taken to protect investors and the integrity of the securities market. Accordingly, the Committee issues the following interim directions:
 - a. The Noticee is prohibited from registering new clients in all segments with immediate effect until further direction.

 - b. The Noticee is directed to take corrective actions, including re-KYC of the non-compliant client accounts and provide compliance certificate duly certified by a Chartered Accountant to the satisfaction of the Exchange within 45 days.

Sd/-
Mona Bhide
(Chairperson)

Sd/-
K Narasimha Murthy
(Committee Member)

Sd/-
S Ravindran
(Committee Member)

Sd/-
Ranganayakulu Jagarlamudi
(Committee Member)

Sd/-
Ashishkumar Chauhan
(Committee Member)

Date: February 20, 2023