



**Before the
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 January 18, 2022**

In the matter of Trading Member M/s. Indianivesh Shares and Securities Pvt. Ltd.

CORAM:

| | |
|------------------------|--------------------|
| Ms. Mona Bhide | - Chairperson |
| Mr. K Narasimha Murthy | - Committee Member |
| Mr. Vikram Limaye | - Committee Member |

ALSO PRESENT:

| | |
|-----------------------|----------------------------------|
| Ms. Priya Subbaraman | - Chief Regulatory Officer |
| Dr. Dinesh Kumar Soni | - Sr. Vice President, Regulatory |
| Mr. Suresh Nair | - Vice President – Enforcement |

BACKGROUND

1. M/s. Indianivesh Shares and Securities Pvt. Ltd. ("Noticee") is a member registered with the National Stock Exchange of India Limited ("Exchange") and enabled for trading in the Capital Market ("CM") and Futures & Options ("F&O") segments since December 2006 and Currency Derivatives ("CD") segment since August 2008.
2. The Exchange conducted an inspection of the books of accounts and records of the Noticee on March 27, 2020. Post-inspection, on analysis of the data, the Exchange observed that the Noticee had misused the clients' funds for meeting the pay-in obligations of other clients resulting in a shortfall of clients' funds involving Rs.93.26 crores. Furthermore, the Exchange observed that the Noticee had misused the funds of credit balance clients for meeting the margin obligations of debit balance clients involving Rs.99.43 crores.
3. As of April 14, 2020, the Exchange received 846 investor complaints involving Rs.31.44 crores. Hence, the Exchange, vide email dated April 30, 2020, directed the Noticee to resolve all the pending investor complaints and file a weekly compliance report/status of

Regd. Office : National Stock Exchange of India Limited | Exchange Plaza, C-1, Block G, Bandra Kurla Complex, Bandra (E), Mumbai – 400 051,
India +91 22 26598100 | www.nseindia.com | CIN U67120MH1992PLC069769

This is an electronic letter which does not require a signature

Page 1 of 33

the direction. However, the Noticee failed to comply with the said direction. Further, the Noticee vide its email dated March 30, 2020, requested for voluntary disablement of the terminals in all segments

SHOW-CAUSE NOTICE

4. The Exchange issued a show-cause notice bearing reference No. NSE/INSP/CMFOCDS/LPI/19-20/SC/12566 dated April 29, 2020 ("SCN"), to the Noticee for the following violations:
 - a. Improper use of clients' funds
 - i. Use of funds of credit balance client for meeting the settlement obligations of debit balance clients resulting in a shortfall of clients' funds involving Rs.93.26 crores.
 - ii. Use of funds of credit balance clients for meeting the margin obligations of debit balance clients involving Rs.99.43 crores.
 - b. Non-resolution of 846 investor complaints involving Rs.31.44 crores.
5. The Exchange advised the Noticee to submit its reply to the SCN by May 9, 2020. The Noticee, vide email dated May 9, 2020, sought an extension of three weeks to reply to the SCN. The Exchange, vide email dated May 12, 2020, granted the Noticee an extension of three weeks to file its reply to the SCN.
6. The Noticee, vide email dated May 15, 2020, requested the Exchange for the following:
 - a. Inspection and copies of the records/documents relied upon in the SCN
 - b. Documents and material relied upon by the Exchange over and above the documents submitted by the Noticee in reply to the Exchange's request dated March 30, 2020
 - c. Any internal reports/analysis charts prepared by the Exchange preceding the SCN
 - d. Report on Forensic Audit prepared by KPMG
 - e. Investors' complaints referred in the SCN
 - f. Any other documents that the authority referred to and relied upon
7. The Noticee, vide email dated May 18, 2020, submitted a detailed settlement proposal of all investor complaints. Subsequently, the Noticee, vide email dated May 21, 2020, requested the Exchange for the following:

- a. To keep the SCN in abeyance in view of the settlement proposal and request for inspection and copies of records/documents relied upon in the SCN.
 - b. To permit the Noticee to submit its reply to the SCN if the same becomes necessary upon the outcome of the settlement proposal, or in the alternative grant the Noticee an inspection and copies of the documents, and a further period of one week from the date of inspection and furnishing copies of documents.
8. The Exchange, vide email dated May 26, 2020, provided the inspection report and list of pending investor complaints to the Noticee. The Exchange informed the Noticee that it had placed reliance upon the documents/data submitted by the Noticee during the inspection and not the forensic report for the SCN. The Exchange advised the Noticee to resolve all pending investor complaints immediately and reply to the said SCN by June 2, 2020, without further delay.
9. In reply to the Noticee's email dated May 30, 2020, the Exchange, vide email dated June 5, 2020, clarified that the settlement proposal is independent of the SCN and has no relevance for explaining the inspection observations.
10. The Noticee, vide email dated September 1, 2020, submitted its reply to the SCN as under:
- a. The SCN and the entire proceedings before the MCSGFC are pre-mediated.
 - b. The documents forming the basis of the SCN cannot be relied upon.
 - c. The complaints, forming the basis of the SCN, were not provided, and the Noticee has settled disputes with the investors.
 - d. The Noticee has relied upon the stand taken by the Exchange in Commercial Arbitration Petition No. VC-LD_No.47 of 2020 filed before the Hon'ble Bombay High Court, and the substantial issue is pending before the Hon'ble High Court in the said petition.
 - e. The SCN is premature, and the Noticee has outlined the brief facts and circumstances that led to the issuance of the SCN.
 - f. The Noticee has relied upon specific contentions, which the Noticee claims to be the essential points to consider whether there is any merit in the SCN.
 - g. The Noticee has relied upon the settlement/withdrawal of complaints against the Noticee. Apart from the above, the Noticee has also relied upon certain miscellaneous grounds.

11. The Noticee, vide email dated September 29, 2020, submitted an addendum to the reply dated September 1, 2020, to the SCN. The Noticee informed the Exchange that it had settled all the pending investor complaints. Hence, the SCN does not stand and ought to be withdrawn or set aside. The Noticee submitted that the transaction of lending/funding between the Clearing Member, Edelweiss Custodial Services Ltd. ("ECSL") and the Noticee was independent of the Trading Member - Clearing Member arrangement. The said transaction cannot be considered for calculating the value of 'G' (availability of client funds) as per the Enhanced Supervision of Stockbrokers. The Noticee, therefore, contended that it had two independent and mutually exclusive transactions with ECSL. The first transaction was a transaction in the capacity of a Trading Member – Clearing Member relation. The Noticee acted as the Trading Member in this transaction, and ECSL acted as a Clearing Member. The second transaction, being independent of the first transaction, was a funding transaction, where ECSL covered the settlement obligations of the Noticee for 18% interest.

SUPPLEMENTARY SHOW-CAUSE NOTICE

12. The Exchange carried out a forensic audit of the books of accounts and data/information submitted by the Noticee through KPMG, external auditor. Based on the findings of the forensic audit, the Exchange issued a supplementary show-cause notice bearing reference No. NSE/INSP/CMFOCDS/20-21/SC/12566 dated November 10, 2020 ("Supplementary SCN"), to the Noticee for the following non-compliances:
- Engagement as a principal in a business other than that of securities involving personal financial liability in the case of 3 related parties involving Rs.72.19 crores.
 - Use of clients' securities for purposes other than specified involving securities worth Rs.40.39 crores
13. The Noticee, vide email dated November 26, 2020, replied to the Supplementary SCN and submitted the preliminary objections to the maintainability of the Supplementary SCN. The Noticee submitted that the allegations are false, baseless, incorrect and contrary to the records for the reasons stated in the reply.

PROCEEDINGS BEFORE MCSGFC

MCSGFC meeting held on June 16, 2020

14. The Noticee did not avail the opportunity for a personal hearing before the MCSGFC on June 16, 2020; instead, vide email dated June 11, 2020, requested the Exchange to keep the SCN in abeyance. The Noticee sought an adjournment on the grounds that the SCN was based on investor complaints and the Noticee was in the process of settling the investor complaints. The Noticee sought time till June 30, 2020, to resolve all investor complaints.
15. The Committee noted that the Noticee resolved investor complaints involving Rs.58.83 crores. The Noticee provided undertakings given by the investors containing the unconditional withdrawal of the complaints by the investors.
16. Upon considering the facts and circumstances of the case, the Committee issued the following directions:
 - a. The Noticee shall continue to remain disabled across all segments till further notice.
 - b. The Noticee shall recoup the shortfall of clients' funds within 2 months from the date of the direction and submit documentary evidence to the Exchange.
 - c. The Noticee shall settle the investor complaints within 2 months from the date of the direction.
 - d. The Noticee shall submit its response, if any, to the SCN within 1 month from the date of the direction.

The Exchange vide email dated July 27, 2020, forwarded the interim order dated July 27, 2020, to the Noticee.

MCSGFC meeting held on January 12, 2021

17. The Exchange vide email dated January 5, 2021, granted the Noticee an opportunity of personal hearing before the Committee in its meeting held on January 12, 2021. Mr. Rajesh Nuwal, Director and Mr. Jinesh Doshi, Legal Advisor, on behalf of the Noticee, appeared for the personal hearing through video conferencing. The Noticee's representatives, while reiterating their submissions made in response to the SCN and Supplementary SCN, also made the following oral submissions:
 - a. The Noticee seeks one more opportunity to restart its business, post-clearance of its dues.
 - b. In accordance with its action plan submitted to the Exchange, the Noticee settled majority of its clients.

- c. The Noticee paid HDFC Bank and will resolve the ECSL legal issue within one or two months.
 - d. No investor complaints are pending against the Noticee with the depositories/stock exchange.
 - e. There were no disciplinary proceedings initiated against the Noticee by regulators in the past.
 - f. The Noticee kept fixed deposits to the tune of Rs.100 crores with ECSL towards client margin, which belonged to its clients. When the Court gave the status quo, the Noticee resolved the matter in weeks.
 - g. Due to the market fall of 12000 points, clients' liquid financial assets and collaterals deteriorated drastically in those 15 days of March 2020.
 - h. The Noticee accepts that there were some omissions and violations in ensuring compliance with the regulatory requirements of the Exchange/SEBI. The only fault of the Noticee was that the liquid financial assets of the Noticee were lying in the form of equity. Since equity got wiped off, the Noticee faced financial problems. The Noticee has always ensured that the funds payable to the creditors are available at all times. The ledgers and other financial documents prove that the Noticee has not diverted the funds. From the audited financials of the Noticee, it is evident that there were no loan transactions between related parties.
 - i. The Exchange auditors considered only the back-office software data of the Noticee. The Noticee has two software – Tally and Liddha Diddha (LD). The Noticee, while preparing the financials, always considers the consolidated figures of both software. However, the Noticee could not explain this to the auditors due to insufficient staff. Hence, in its reply to the SCN, the Noticee submitted the correct figures and balances with merged accounts and audited financials to substantiate its claim.
 - j. The Noticee has closed all its other businesses to revive this broking business.
18. The Committee noted that 11 investor complaints involving Rs.18.21 lakhs were pending against the Noticee as of January 5, 2021. Upon considering the Noticee's submissions and the fact that the Noticee had resolved a majority of the investor complaints and is currently disabled, the Committee decided to grant some more time to settle the remaining investor complaints.
19. The Exchange vide email dated January 12, 2021, forwarded the interim directions to the Noticee.

MCSGFC meeting held on April 30, 2021

20. The Committee noted the following developments that transpired after January 12, 2021:
- The Noticee settled its clients and requested for enablement of its trading terminals.
 - The arbitration matter between ECSL, HDFC Bank, and the Noticee is pending before the Hon'ble Bombay High Court.
21. Upon considering the above, the Committee deemed it necessary to examine the balance sheet and the net worth of the Noticee. Therefore, the Committee directed as under:
- The Noticee shall submit -
 - Audited annual accounts as of March 31, 2021
 - Net worth certificate as of March 31, 2021, duly certified by a Chartered Accountant (after considering liabilities towards the clients from whom NOCs have been received) along with supporting documents for verification.
 - Updated status of settlement of clients.
 - The Noticee shall continue to be disabled in all segments until further notice.
22. The Exchange vide email dated April 30, 2021, forwarded the interim directions to the Noticee. The Noticee vide emails dated May 25, 2021, and June 30, 2021, sought an extension to submit the documents described above.

MCSGFC Meeting held on August 23, 2021

23. The Committee noted the further developments that transpired after April 30, 2021-
- The Noticee, vide email dated July 27, 2021, submitted the audited annual accounts as of March 31, 2021, and the net worth certificate as of March 31, 2021, duly certified by a Chartered Accountant (after considering liabilities towards the clients from whom NOCs have been received) along with supporting documents for verification.
 - The Noticee's net worth is (-) Rs.50.01 crores as of March 31, 2021.
 - The Auditors raised several concerns because of the accumulated losses, uncertainty on the timelines for resumption of the operations and substantial erosion of net worth.
24. The Noticee, vide the said letter July 27, 2021, also submitted that it has initiated the necessary steps to recoup the networth viz. recovery of debts, by way of sale of the

shares of their subsidiary company Sansaar Housing Finance Ltd. and introduction of capital by the Promoter in the form of debt/equity/convertible instrument.

25. The Committee also noted the status of settlement of clients' accounts as under:
- Out of the total client payables of Rs.119.19 crores of 9490 clients, the Noticee assured to obtain NOC from 20 clients involving Rs.84.58 crores.
 - Out of the 20 clients involving Rs.84.58 crores, for whom the Noticee had promised to submit NOCs, the actual NOCs were submitted for only 17 clients amounting to Rs.60 crores. The Noticee has settled the NOC clients also over a period of time. At present, the Noticee is to settle to 3 clients involving Rs.1.84 crores, who have given NOCs.
 - The Noticee settled 8984 clients involving Rs.36.56 crores. The Noticee could not settle the remaining 486 clients involving Rs.0.05 crores due to invalid bank details/NRE code.
 - There are no investor complaints pending against the Noticee as on date.
26. The Committee also noted as under-
- The Noticee misused the funds of credit balance clients to meet the settlement obligation of debit balance clients resulting in a shortfall of funds of Rs.93.26 crores. The Noticee further misused the funds of credit balance clients to meet the margin obligations of debit balance clients to the tune of Rs.99.43 crores.
 - The Clearing Member of the Noticee, ECSL, sold client securities worth Rs.40.39 crores as the Noticee could not fulfill its obligations. Therefore, the Noticee had misused the client securities as the Noticee cannot utilize the client securities for any purposes other than those specified.
 - The Noticee had misused client assets to the tune of more than Rs.100 crores, discussed in detail as above. It is, therefore, a matter of record that the Noticee has completely failed to ensure that the client assets are not misused. However, the Committee finds that the Noticee has settled all the investors subsequently and submitted the proof thereof.
 - The net worth of the Noticee is (-) Rs.50.01 crores as of March 31, 2021, which is below the minimum net worth prescribed for Trading Members by the Exchange. Rule 33 under Chapter III of NSEIL Rules prescribes that in the event of failure to meet the minimum net worth, the trading membership shall be liable to be terminated.

27. The Committee finds that-
- The Noticee, vide letter dated July 27, 2021, submitted the plan of action for completely recouping the net worth by October 2021.
 - It is also submitted to the Exchange that the Noticee is in the process of recouping the shortfall in networth.
 - No investor complaints are pending for redressal at the Exchange.
 - The Noticee's operations are suspended for more than a year, and over the period the Noticee has settled all clients. The arbitration matter between ECSL, HDFC and the Noticee was sub-judice and pending before the Bombay High Court.

FURTHER DEVELOPMENTS IN THE MATTER POST MCSGFC DATED AUGUST 23, 2021.

28. The Noticee vide email dated November 24, 2021, informed the Exchange that the net worth of the Noticee as on November 11, 2021, has become positive to the tune of Rs.10.51 crores. The Noticee informed to have recouped the net worth by debtor recovery, sale of the subsidiary company and introduction of capital by the Promoter.
29. The Noticee vide email dated December 16, 2021, informed the Exchange as under-
- That it has fully resolved all disputes with its Clearing Member, ECSL and their Banker viz; HDFC Bank Limited; by making full and final payment to both parties. Noticee has submitted a copy of the Settlement agreement entered with ECSL and payment proof of Rs.93.50 crores.
 - That as of today, no complaints remain outstanding against the Noticee, and all disputes of stockbroking operations are fully resolved.
 - The net worth requirement has been complied with, and a copy of the net worth certificate certifying a net worth of Rs.11.99 crores as of December 15, 2021, has been submitted.
 - Since no complaints or disputes remain outstanding, the Noticee hereby requests to withdraw its voluntary disablement of trading terminals and dispose of the SCN proceedings.
 - The Noticee seeks a personal hearing in the matter.

PRESENT PROCEEDINGS BEFORE MCSGFC HELD ON 18TH JANUARY 2022

30. The Exchange vide email dated January 12, 2022, granted the Noticee an opportunity of personal hearing before the Committee. Mr. Rajesh Nuwal and Mr. Dinesh Nuwal,

Director/Promoter, Mr. Kaushik Shah, Director and Mr. Jinesh Doshi, Authorised Representative attended the meeting through Microsoft Teams (by video conferencing) from their respective location(s) on behalf of Indianivesh. The representatives of the Noticee, while reiterating the submissions made in its written responses dated September 1, 2020, and November 26, 2020, also made the following oral submissions-

- a. The Noticee was able to fulfill its commitments to the Exchange and SEBI regarding the settlement of investor claims.
- b. The Noticee applied for voluntary disablement on March 30, 2020, and on May 16, 2020, it submitted a proposal for settlement of retail clients. By July 7, 2020, the Noticee settled all the retail clients. Hence there was a period of more than 3 months when the clients could not be settled due to shortage of funds. By March 2021, the Noticee finalized the matter with ECSL for complete settlement. However, due to COVID and some legal issues, it got delayed. However, ECSL has now been settled completely.
- c. 20 clients had given "No dues" certificates. All these 20 clients have been paid, except 1 client of Rs.35 lacs (approx.), who will be settled in the next ten days.
- d. The Noticee had settled the clients from the additional capital introduced in the Company.
- e. The entire debacle happened due to the market fall because of the COVID 19 pandemic.
- f. Despite the pandemic situation prevalent in the country, the Noticee settled all the clients, Clearing Member and bankers completely in the last two years. At present, no investor complaints are pending against the Noticee.
- g. Given the above, the Noticee requests the Committee for enablement of its trading terminals.

REPRESENTATION RECEIVED FROM THE NOTICEE POST PERSONAL HEARING

31. The Noticee, post the personal hearing before the Committee, also submitted additional representation vide its email dated January 27, 2022, *inter alia* submitting as under-
 - a. The Noticee reiterates that it has not used funds of credit balance clients as alleged or otherwise but has availed finance from ECSL. Thus, the allegation of misuse of client funds is contrary to the facts on record hence untenable/unsustainable.
 - b. As of date, no investor complaints are pending, and it has fully settled dues of its Clearing Member, ECSL, and its bankers.
 - c. The Noticee has been positively engaging with financial institutions to avail banking facilities to restart its business. Further, the Noticee has been interacting with its corporate customers and HNI clients to restart the business.

- d. Given the above, its revival plans will be at great peril if penalized with any form of suspension.
- e. The Noticee has already been in voluntary disablement for a substantial period and is willing to continue voluntary disablement for a further period of upto 45 days.

RELEVANT REGULATORY PROVISIONS

32. At the outset, it is appropriate to refer to the relevant regulatory provisions alleged to have been violated by the Noticee, extracts whereof are reproduced below:

a. Rule 8(3)(f) of Securities Contracts (Regulation) Rules, 1957

8. The rules relating to admission of members of a stock exchange seeking recognition shall inter alia provide that:

(3) No person who is a member at the time of application for recognition or subsequently admitted as a member shall continue as such if -

(f) he engages either as principal or employee in any business other than that of securities or commodity derivatives except as a broker or agent not involving any personal financial liability.

b. Regulation 4.5.3 (e) of NSEIL Regulations (CM and F&O Segments)

No Trading Member or person associated with a Trading Member shall make improper use of the constituent's securities or funds.

c. Exchange Circular No. NSE/INSP/10605 dated April 21, 2008

Brokers should have adequate systems and procedures in place to ensure that client collateral is not used for any purposes other than meeting the respective client's margin requirements / pay-ins. Brokers should also maintain records to ensure proper audit trail of use of client collateral.

d. SEBI Circular No. CIR/MIRSD/18/2011 dated August 25, 2011

The stockbrokers and sub-brokers shall take adequate steps for redressal of grievances within one month from the date of receipt of the complaint and keep the investor/stock exchange(s) duly informed of the action taken thereon. Failure to comply with the said requirement will render the stockbroker liable for penal action.

e. Exchange Circular No. NSE/INSP/29096 dated March 11, 2015

Members are advised to ensure that the funds & securities available in the client bank/s and client beneficiary account/s together with balances available with clearing Member and funds with clearing corporation are not less than the funds and securities payable to the client at all times.

f. Exchange Circular No. NSE/INSP/33276 dated September 27, 2016

3.3.1 *Funds of credit balance clients used for settlement obligation of debit clients or own purpose*

Principle 1

The total available funds, i.e. cash and cash equivalents, with the stockbroker and with the clearing corporation/clearing member (A + B), should always be equal to or greater than Clients' funds as per ledger balance (C)

3.3.2 *Funds of credit balance clients used for Margin obligations of debit balance clients and proprietary trading:*

The clients' funds lying with the clearing corporation/clearing member should be less than or equal to sum of credit clients' margin obligations (MC) and free collateral deposits available with the clearing corporation/clearing member (MF)

If value of G is negative (i.e. $A+B < C$), then fund lying with the clearing corporation/ clearing member (B) is entirely clients' fund. In such cases, B is compared with Margin obligations of credit balance clients and the free deposits available with the clearing corporation/ clearing member. The value of J is calculated as under:

$$J = B - (MC + MF)$$

CONSIDERATION OF THE OBSERVATIONS/VIOLATIONS, THE REPLY OF THE NOTICEE TO THE SCN AND THE FINDINGS OF THE COMMITTEE

33. The following are the observations/violations, the replies of the Noticee dated September 1, 2020, and September 29, 2020, to the SCN, and the findings of the Committee:

33.1 Improper use of client funds

- a. On verification of the data submitted towards weekly monitoring of clients' funds under the Enhanced Supervision of Stock Brokers as of March 30, 2020, the Exchange observed that the Noticee had used the funds of credit balance clients for meeting the settlement obligations of debit balance clients, thereby resulting in a shortfall of clients' funds of Rs.93.26 crores. Thus, the Noticee had violated Principle 1 of the Enhanced Supervision of Stockbrokers. Furthermore, the Noticee had also used the funds of the credit balance clients to the tune of Rs.99.43 crores for meeting the margin obligations of the debit balance clients. Thus, the Noticee had violated Principle 3 of the Enhanced Supervision of Stockbrokers. The details are as per Table 1 and 2 below:

Table 1: Funds of credit balance clients for meeting the settlement obligations of debit balance clients

| Sr. No. | Particulars | Amount (Rs. in crores) |
|---------|--|---------------------------|
| 1 | Total of day end balance in all client bank accounts | 2.14 |
| 2 | Total of day end balance in all own bank accounts | 0.08 |
| 3 | Collateral deposited with Exchanges and Clearing Corporation in the form of cash and cash equivalents | 34.29 |
| 4 | Collateral deposited with Clearing Member (Edelweiss Custodial Services Ltd-ECSL) in the form of cash and cash equivalents | 93.21 |
| 5 | Total credit balance of all clients | 127.19 |
| 6 | Total debit balance of all clients | 130.94 |
| 7 | Edelweiss Custodial Services Ltd. (ECSL) ledger balance | (95.79) |
| | DIFFERENCE (G) | (93.26) |
| | Funds of creditor client's used for another client's in debit by the Noticee | 93.26 |

Table 2: Funds of the credit balance clients used for meeting the margin obligations of the debit balance clients

| Sr. No. | Particulars | Amount (Rs. in crores) |
|---------|-------------|---------------------------|
|---------|-------------|---------------------------|

| | | |
|---|--|--------------|
| 1 | Collateral deposited with Exchanges and Clearing Corporations in form of cash and cash equivalents (A) | 34.29 |
| 2 | Collateral deposited with Edelweiss Custodial Services Ltd in form of cash and cash equivalents (B) | 93.21 |
| 3 | Margin utilized for positions of credit balance Clients (C) | 0.62 |
| 4 | Free/unblocked collateral deposited with Clearing Corporations (D) | 27.45 |
| 5 | Free/unblocked collateral deposited with ECSL (based on collateral report of ECSL) (E) | - |
| | Funds of credit balance clients used for margin obligations of debit balance clients by the Noticee (A+B-C+D+E) | 99.43 |

- b. In its reply to the SCN, the Noticee, vide its email dated September 1, 2020, submitted as under:

Submissions with respect to violation of Principle 1 of Enhanced Supervision

Finding of 'G' is incorrect and erroneous

The collaterals deposited with the Clearing Member, i.e. ECSL shown as Rs.93.21 crores (Table 1, Sr. No. 4) is incorrect, and the correct amount is Rs.100.75 crores. This amount is towards client credit only.

The deduction of Rs.95.79 crores due to the ECSL ledger balance (Table 1, Sr. No.7) is incorrect and contrary to the Enhanced Supervision circular. The amount cannot be considered for calculating "G" as per the Enhanced Supervision circular. The Noticee provided reasons for not deducting the outstanding unsecured balance of Rs.95.79 crores as under:

The fixed deposit lying with ECSL was issued by HDFC Bank Ltd. in favour of "NCL – A/c Edelweiss Custodial Services Limited" and was subsequently submitted to NSE Clearing Limited ("NCL") by ECSL. The fixed deposits were issued pursuant to the Tripartite Agreement between the Noticee, ECSL and HDFC Bank Ltd. The Tripartite Agreement clearly mentions the purpose and intent of the fixed deposit, i.e. fixed deposit is towards margin requirements with NCL and not towards settling any other claim of the Clearing Member against the Noticee.

It is the stand of the Noticee, backed by record and law, that the amounts forming a part of the fixed deposits are in the nature of collaterals. However, ECSL is claiming the fixed deposits towards its claims against the Noticee. Due to the illegal and erroneous claims made by ECSL, the nature of monies maintained as fixed deposits is a subject matter of the dispute before the Hon'ble Bombay High Court in the Arbitration Petition filed by ECSL against the Noticee and HDFC Bank Ltd. The Exchange has made an application to implead itself in the petition. The fact that the Exchange intervened in the proceedings to claim the fixed deposits to secure the interest of investors makes it very clear that the fixed deposits belong to the investors.

The reporting format of the Exchange/SEBI clearly states that collaterals available with the Exchange/Clearing Member are to be considered towards clients' credit balance. In accordance with the said format, the collaterals equivalent to Rs.100.75 crores in the form of fixed deposits issued by HDFC Bank Ltd. are lying with the ECSL. These amounts should be considered for credit balance clients instead of deducting the same with the debit balance of ECSL, which is a separate unsecured loan arrangement between ECSL and the Noticee for funding the settlement obligations of the Noticee.

The debit balance ledger of ECSL reflects the amount owed by the Noticee to ECSL towards a separate unsecured loan arrangement between the Noticee and ECSL for funding the settlement obligations of the Noticee. ECSL charges interest @18% p.a. There is no lien and cannot be any lien of ECSL on the fixed deposits deposited with ECSL as a Clearing Member to the tune of Rs.100.75 crores, and these amounts ought to be utilized for the benefit of the investors.

Thus, after considering the collateral deposited with ECSL as Rs.100.75 crores instead of Rs.93.21 crores and not reducing the amount of Rs.95.79 crores towards the unsecured loan, there is no shortfall of client funds to meet the client payables. The revised working of Principle 1 i.e., Client funds used for meeting pay-in obligations of other clients, is as per Table 3 below-

Table 3- Revised calculation for Client funds used for meeting pay-in obligations of other clients (Principle 1 of the Enhanced Supervision)

(Rs. In crores)

| Particulars | Amount as per SCN | Amount as per Noticee's Calculation |
|---|-------------------|-------------------------------------|
| Total of day end balance in all Client Bank Accounts | 2.14 | 2.14 |
| Total of day end balance in all Own Bank Accounts | 0.08 | 0.08 |
| Collateral deposited with Exchanges and Clearing Corporation in form of Cash and Cash Equivalents | 34.29 | 34.29 |
| Collateral deposited with Clearing Member ECSL, inform of Cash and Cash Equivalents | 93.21 | 100.75* |
| Total Credit Balance of all clients | 127.19 | 127.77 |
| Total debit balance of all clients | 130.94 | 131.25 |
| Edelweiss Custodial Services Ltd. (ECSL) Ledger Balance | (95.79) | - |
| DIFFERENCE (G) G= (A+B)-C | (93.26) | 9.49 |
| Funds of one client used for another client | 93.26 | - |

Submissions with respect to violation of Principle 3 of Enhanced Supervision

The value of 'J' cannot be looked at since 'G' is incorrectly calculated

As per Enhanced Supervision circular, clients' funds utilized towards margin obligations of debit balance clients and proprietary margin obligations are considered as a violation of Principle 3 and denoted as 'J'. The value of 'G' as calculated under Principle 1, materially determines the effect on 'J'.

The value of 'G' is incorrectly noted as negative in the SCN, whereas the calculation of 'G' is positive. The value of 'G' being positive, the manner of calculation of 'J' would materially differ, and hence the value of 'J' as per the said SCN is incorrect. The Noticee provided the revised Table as under:

Table 4- Revised calculation for Client funds used for meeting margin obligations of debit balance clients (Principle 3 of the Enhanced Supervision)

| Sr. No. | Particulars | Amount (Rs. in crores) |
|---------|--|------------------------|
| C | Credit balance clients | 127.77 |
| A | Total of client bank balance (client & settlement account) | 2.22 |
| MC | Margin deposit utilized for granting exposure to credit balance clients | 0.63 |
| MF | Free margin deposits with the Exchange (unutilized collateral lying with the Clearing Corporations/Clearing Member [(i) Before Haircut, (ii) After Haircut]) | (i) 156.12 |
| | | (ii) 126.28 |
| | Difference(J) J= (C- A)-(MC+MF) | -31.20 |
| | | -1.36 |

Therefore, as on March 30, 2020, the value of 'J' is in compliance with the principles of Enhanced Supervision of Stockbrokers.

- c. In its reply to the SCN, the Noticee, vide email dated September 29, 2020, submitted as under:
- i. The transaction of lending/funding between ECSL and the Noticee was independent of the Trading Member – Clearing Member arrangement, and the same cannot be considered for calculating the value of 'G' as per the Enhanced Supervision circular.
 - ii. The Noticee had two independent and mutually exclusive transactions with ECSL. The first transaction was in the capacity of a Trading Member - Clearing Member relation. The second transaction, being independent of the first transaction, was a funding transaction, where ECSL covered the settlement obligations of the Noticee for 18% interest.
 - iii. ECSL is claiming the fixed deposits pursuant to the Tripartite Agreement against the settlement obligations of the Noticee arising out of the second transaction against the Noticee.
 - iv. The claims made by ECSL are a subject matter of the proceedings initiated by ECSL, which are pending in the Hon'ble Bombay High Court (VC-LD No. 47 of

2020). Thus, the amount claimed is subject to the outcome of the proceedings and reconciliation. Further, the amount is subject to adjustment / set off against the claim which the Noticee will have against ECSL.

d. The Committee finds as under-

- i. The contention of the Noticee that the SCN violates principles of natural justice on the grounds that it is pre-mediated, is incorrect and lacks merit. The SCN affords an opportunity to the Noticee to refute the charges levelled against the Noticee in the SCN and, therefore, meets the principles of natural justice. The contention of the Noticee that the issuance of an SCN is a pre-meditated act is therefore vague and made without an appropriate understanding of the quasi-judicial process.
- ii. The contention that the documents forming the basis for the SCN cannot be relied upon since the said documents were full of inconsistencies and inaccuracies, is wrong. It is observed that apart from making an allegation of inconsistencies and inaccuracies in the minutes of the meeting dated April 3, 2020, which took place between the Noticee and Exchange officials, the Noticee does not seem to have any other valid and substantive ground to demonstrate why these minutes/documents cannot be relied upon.
- iii. The minutes of the meeting do not even form part of the documents relied upon for the purpose of issuance of the SCN to the Noticee. Further, the charges leveled against the Noticee in the SCN were based on the observations mentioned in the inspection report. Therefore, any inconsistencies ought to have been brought out as a specific explanation to the charge rather than making false statements. It is also pertinent to observe that the email dated May 26, 2020, specifically clarified that the Exchange has relied upon documents/data submitted by the Noticee only, which have been submitted during the inspection and hence it is amply clear that the stated minutes of the meeting held on April 3, 2020, was not relevant for the purpose of SCN.
- iv. The Noticee's contention is that the complaints filed with NCDEX forming the basis of the SCN were not provided and the disputes with the investors were settled, and therefore the SCN is illegal, bad and cannot be sustained in law. The initiation of an action based on the information received from other MIIs and the consequential action is a part of the course of regulatory measures required to be taken by the MIIs to discharge its regulatory obligations. Further, the complaints filed with

- NCDEX were the trigger point to initiate an inspection. The violations observed during the inspection and mentioned in the SCN are independent of the complaints filed with NCDEX. Hence the Noticee's contention is not tenable.
- v. The Committee finds that the stand taken by the Noticee in the interim application filed before the High Court is not germane to the proceedings before this Committee while adjudicating the charges of misuse of client funds. Further, the contention of the Noticee that the issues raised in the SCN revolve around the margin monies kept in the form of fixed deposits with ECSL is inexplicable because the funds that were available with Clearing Member (ECSL)/Clearing Corporation were insufficient to meet the client payables.
- vi. The Noticee, in its email dated January 27, 2022, contended that it has not used funds of credit balance clients as alleged or otherwise, but have availed finance from ECSL. The Noticee has further claimed that the allegation of misuse of client funds is contrary to the facts on record, hence untenable/unsustainable. This claim of the Noticee is a clear afterthought because if there was no shortage of client funds, then the Exchange would not have received hundreds of investor complaints against the Noticee. Further, there would have not been any need for the Noticee to apply for voluntary disablement of its terminals and later submit an action plan for settlement of clients, including NOCs submitted on behalf of clients. It is a fact that it took nearly a year for all the Exchanges to coordinate with the Noticee for settlement of client assets. The details of clients' shortages have been dealt in detail in the paragraphs below.
- vii. The contention that the SCN is premature is absurd, devoid of any merits and made without appreciating the regulatory concerns arising from the observation of shortage of client funds leading to a potential default. The regulatory actions for the protection of investors' assets stem from such critical observations and its equally important to also afford an opportunity to explain why the issuance of SCN is essential. Thus, the SCN sets the regulatory action in motion and cannot be termed as premature.
- viii. Regarding the Noticee's contention that the computation of 'G' as of March 30, 2020, is incorrect, and therefore the value of 'J' is also incorrect, it is observed that Exchange circular No. NSE/INSP/33276 dated September 27, 2016, on Enhanced Supervision, enumerates three principles for monitoring of clients' funds lying with the stockbrokers. Out of the three Principles, Principle 1 requires the Members to

ensure that the total available funds i.e., cash and cash equivalents with the stockbroker and with the Clearing Corporation/clearing member (A + B) should always be equal to or greater than Clients' funds as per client payables in Member's books (C). The value of (G) is computed by deducting the total client payables from the total funds available with the Member and Clearing Member/Clearing Corporation. If negative, the value of G indicates that the funds available with the Member are insufficient to meet the client payables. As per Principle 3, the value of 'J', if positive, indicates the extent of clients' funds utilized towards margin obligations of debit balance clients and proprietary margin obligations. This value of 'J' acts as an alert to the Stock Exchanges on the possible misuse of clients' funds towards margin obligations of debit balance clients and proprietary margin obligations.

- ix. The Noticee's contention that the Exchange has wrongfully deducted Rs.95.79 crores, contrary to the Enhanced Supervision circular, is flawed. From the Circular, it is sufficiently clear that any money lying with the Clearing Member/Clearing Corporation and with the Trading Member in the client bank account should be more than the client payables. It is observed from the records that the Clearing Member report indicated a negative balance which reflects the non-availability of funds with the Clearing Member to meet the Noticee's own/clients' trading obligations. The fact that the negative (debit) balance was mentioned in the Clearing Member report proves that it was not a separate line of credit as claimed by the Noticee.
- x. Regarding the Noticee's contention that the correct amount of collaterals deposited with the Clearing Member at Table 1, Sr. No.4 is Rs.100.75 crores and not Rs.93.21 crores, it is observed from the records that the Clearing Member's report itself indicated the deposits as Rs.93.21 crores which the Exchange has considered for the purpose of computation. Therefore, the said contention of the Noticee is incorrect.
- xi. Therefore, it is evident that the Noticee did not have sufficient funds and hence the Committee agrees with the observation that there was a shortage of client funds to meet the client payables as of March 30, 2020. Essentially, credit balance clients' funds were used for settlement obligation of debit balance clients/own purposes by the Noticee which amounts to co-mingling and misuse of client funds. There was absolute failure of the risk management system by the Noticee. Further, the Noticee did not undertake any due diligence and care in handling the

client assets. This also resulted in immense stress and pain to investors at large as many of them had to wait for more than 6 months for settlement.

- xii. The Committee further notes that the benefit of fixed deposits to the tune of Rs.93.21 crores has already been considered for the purpose of availability of funds before arriving at the shortfall of Rs.93.26 crores as on March 30, 2020. The Committee finds that the Noticee has not explained why the amount of Rs.95.79 crores should not be deducted to arrive at the availability of funds. In the absence of any concrete response, no benefit can be extended. Accordingly, the Noticee's contention that the value of 'J' is also incorrect as 'G' is incorrectly calculated, therefore, does not hold good.
- xiii. Regarding the Noticee's contention that the complaints were settled and withdrawn, and therefore the SCN needs to be withdrawn cannot be accepted. It is a matter of the fact that there were client shortages that have been settled subsequent to the issue of the SCN. It is also a matter of record that more than 1400 complaints were subsequently settled. The settlement of the complaints is post the interim directions of the Committee. As such, there is no merit to consider the request to recall/withdraw or set aside the SCNs issued by the Exchange.
- xiv. Regarding the Noticee's reliance on the purported tripartite agreement between the Noticee, ECSL and HDFC Bank Ltd. in the matter of fixed deposits that were created and its purpose, as well the contention that the same cannot be used against any claim of ECSL against the Noticee, the Committee finds that the said contention is not germane to the charge of non-availability of client funds and is an inter-se dispute between the Noticee and ECSL and therefore cannot be regarded towards the clear availability of client funds.
34. The following are the alleged observations/violations, the replies of the Noticee dated November 26, 2020, to the Supplementary SCN and the findings of the Committee:
- 34.1 Engagement as a principal in a business other than that of securities involving personal financial liability
- a. On verification of the provisional trial balance for the financial year 2020-21, it was observed that the Noticee had outstanding loans and advances extended to 3 related parties amounting to Rs.72.19 crores as on April 20, 2020. The details of the same are as per Table 5 below:

Table 5 – Details of loans & advances extended by the Noticee to related parties

| Sr.No. | Related Party | Amount (Rs.in crores) |
|---------------|------------------------------------|------------------------------|
| 1 | IndiaNivesh Limited (INL) | 51.95 |
| 2 | IndiaNivesh Capital Limited (INCL) | 11.34 |
| 3 | K L Enterprises | 8.90 |
| | Total | 72.19 |

On further verification, it was observed that the Noticee received interest from K.L. enterprises amounting to Rs.57.58 lakhs and the interest payable by the Noticee to INL and INCL is Rs.76.38 lakhs. On further analysis of loans and advances ledgers of INL and INCL, it was observed that the ledgers of both the companies had a payable balance to the tune of Rs.2.61 crores and Rs.6.21 crores till January 29, 2020, and February 23, 2020, respectively. The Noticee had extended loans and advances from February 2020, till April 20, 2020, to the tune of Rs. 444.12 crores. [INL – Rs.181.83 crores and INCL – Rs.262.29 crores].

- b. In its reply dated November 26, 2020, to the Supplementary SCN, the Noticee submitted as under:
- (i) For the purposes of detailing the transactions, the relationship and the businesses of the related parties are defined as under-
- IndiaNivesh Shares and Securities Private Limited, i.e., the Noticee is a wholly-owned subsidiary of IndiaNivesh Limited (“INL”). INL is a public listed company and a Non-Banking Finance Company (NBFC) duly registered with RBI.
 - The Noticee is a sister concern of IndiaNivesh Capitals Limited ('INCL'). Both INCL and Noticee are subsidiaries of INL. INCL is a public limited company and Non-Banking Finance Company (NBFC) duly registered with RBI.
 - K.L. Enterprises LLP (K.L.) is a Limited Liability Partnership. The Noticee was a Partner of K.L. from July 5, 2019, to October 1, 2019, and had contributed Rs.28.56 crores towards the partners contribution.
- (ii) The Noticee used to borrow funds from INL and INCL for business and working capital requirements.

- (iii) The allegation of the ledger of INL and INCL had a payable balance of Rs.2.61 crores and Rs.6.21 crores on January 29, 2020, and February 23, 2020, is incorrect as the payable balances taken by the Exchange Auditors are incorrect and incomplete.
- (iv) The Noticee has Liddha Diddha (LD) as back-office software and Tally as accounting software. All the entries related to day-to-day business activities were in regular course entered into the LD software, and other entries are entered into Tally software. The entries were merged at the end of quarter/year-end to prepare the financials. It appears that the Exchange Auditor completely failed to consider the data from the Tally software, which led to anomalies in the findings.
- (v) The Noticee vide email dated September 2, 2020, sent a provisional financial statement as of March 31, 2020, along with data from the Tally software to the Exchange Auditor. However, it appears that the data was not considered, and due to such non-consideration of data, the financial statement and entries, the findings are incorrect and incomplete. As entries entered directly in accounting software have not been considered at all, the findings are demonstrably incorrect.
- (vi) On consideration of data from the Tally and LD software, the correct ledger balances are as under-
 - a. The correct credit balance of INL in the Noticee's books was Rs.54.61 crores (loan given by INL to the Noticee) as on January 29, 2020, instead of Rs.2.61 crores as mentioned in the Supplementary SCN.
 - b. The correct credit balance of INCL in the Noticee's books was Rs.67.71 crores (loan given by INCL to the Noticee) as on February 23, 2020, instead of Rs.6.21 crores as mentioned in the Supplementary SCN.
- (vii) The Noticee has submitted copies of audited ledger accounts of INL and INCL from January 1, 2020, till March 31, 2020, highlighting correct credit balances on January 29, 2020, and February 23, 2020, respectively in support of its claim.
- (viii) There are no financial activities (granting of loans), and the statutory auditors of the Noticee never reported any loans given by the Noticee to its holding/fellow subsidiary companies in any related party transactions.
- (ix) The Exchange Auditors have not considered the following transactions:
 - a. Advance payment for the purchase of property to INL
 - 1. The Noticee had entered into a Memorandum of Understanding (MoU) with an entity named M/s. Balashri Commercials Limited (BCL), one of the Promoter entity of the Noticee, to purchase the property situated at

1701 to 1706, 17th Floor, Lodha Supremus, Senapati Bapat Marg, Lower Parel, Mumbai for an aggregate consideration of Rs.55 crores payable by the Noticee.

2. Thereafter, in furtherance to the MoU, BCL requested the Noticee to make the advance payment of the consideration amount to INL. Accordingly, the Noticee had made an advance payment of Rs.52 crores to INL on behalf of BCL on various dates in January 2020.
3. The said MoU was cancelled, and the entire amount of Rs.52 crores was recovered from INL in September 2020.
4. Thus, there is no basis or merit in the allegation that the Noticee had given advances of Rs.181.83 crores to INL. In fact, considering the complete ledger, there are no loans granted by the Noticee to INL.

b. Payment for purchase of shares to INCL

1. The Noticee paid an amount of Rs.11.50 crores as an advance for the purchase of shares of a related entity of INCL, Sansaar Housing Finance Limited. The Noticee had also got the shares transferred in its name in demat mode subsequently.
2. The Noticee has submitted a copy of the share purchase agreement dated January 1, 2020, and demat statements as documentary evidence.

c. Partner's current account receivable from K.L. Enterprises LLP

1. The Noticee was a partner of K.L. Enterprises LLP for a period from July 5, 2019, to October 1, 2019, with a capital contribution of Rs.28.56 crores.
2. The amount of Rs.8.90 crores is the balance of partner's current account that remains receivable from K.L. Enterprises LLP.
3. Interest receivable for Rs.50.39 lakhs (reduced from Rs.57.58 lakhs to Rs.50.39 lakhs due to reduction of interest rate from 8% p.a. to 7% p.a. payable on Partner's Capital Account) from K.L. was interest on Partners Capital Account as per audited books of accounts. There are no loans/funding carried out by the Noticee to K.L. at any point of time as has been alleged in the show-cause notice.
4. The Noticee has submitted a ledger of K.L. Enterprises LLP in support of its claim.

(x) Thus, all the instances mentioned above were neither loans and advances nor any funding activities carried out by the Noticee. All the transactions were in the normal course of business and had approvals from the Board of Directors of the respective Companies backed by duly notarised supporting documents. The books of accounts of the Noticee have also been audited by the Statutory Auditors of the Noticee which reflect a true and fair view of the financial statements of the Noticee and neither of the transactions alleged in the Supplementary SCN are true.

c. The Committee finds as under-

- (i) With respect to the Noticee's contention that it had made an advance payment of Rs.52 crores out of Rs.55 crores towards the sale consideration for the purchase of property, it is observed that the Noticee had submitted a notarised copy of an MoU dated January 1, 2020, executed between BCL and the Noticee. The Noticee also contended that BCL had requested the Noticee to make the advance payment to INL, which is the parent company of the Noticee. The MoU was to be completed by March 31, 2020. The Noticee further claims that the said transaction could not be completed as the trading terminals of the Noticee were disabled as per its own request. The funds have been returned by INL to the Noticee. On perusal of the MoU, the Committee does not find any such arrangement for payment of funds to INL on behalf of BCL for the purchase of the property. Further, though there is a letter from BCL dated January 11, 2020, requesting the Noticee to pay the consideration to INL on behalf of BCL, the Committee does not find any reason recorded for such payment and receipt of funds by any of the parties.
- (ii) With respect to the payment of Rs.11.50 crores to INCL, the Noticee contended that the same was paid to INCL for acquiring the equity shares of Sansaar Housing Finance Limited (formerly known as Indianivesh Housing Finance Limited), an entity promoted by INCL. In support of its claim, the Noticee submitted a copy of the share purchase agreement dated January 1, 2020, executed between INCL and the Noticee. The Noticee also submitted the demat account statement to demonstrate the receipt of those shares in its own demat account. The Committee finds that the said submission of the Noticee is acceptable.
- (iii) With respect to the current account receivable from K.L. Enterprise LLP to the tune of Rs.8.90 crores, the Noticee explained that the said amount was

- a refund that was due to the Noticee towards the capital contribution and is verifiable from the copy of ledger balances of K.L. Enterprises LLP.
- (iv) The Noticee contended that it maintains its records in two software applications, i.e. LD and Tally. All entries for day-to-day business activities are entered into LD and other entries in Tally, and that the entries in both the software are merged at the end of the quarter/year to prepare financials. The Exchange auditor completely failed to consider both the data, leading to anomalies in findings. When the entries from both the software are considered, there will not be any amounts that the Noticee had advanced to INL and INCL. On the contrary, the Noticee owes the amounts to INL and INCL. The Committee finds that the Exchange auditors vide email dated September 7, 2020, informed the Noticee that the cut-off date for submission of data by the Noticee was July 31, 2020, as conveyed vide email dated July 29, 2020. However, as an exception, the Exchange Auditors considered information provided by the Noticee till August 27, 2020. The Exchange auditors have informed the Noticee that any data submitted post-August 27, 2020, was not considered for review by the Exchange auditors. In this regard, the Committee noted that the Noticee, aggrieved by the said action of the Exchange Auditor, has claimed to have approached the Exchange and in a meeting held on September 16, 2020, between the Exchange, the Auditor and the Noticee, the Exchange Auditor was told to accept the same. However, no such directions were given by the Exchange contrary to what is claimed by the Noticee.
- (v) The Noticee, therefore, contended that all the three instances were neither loans and advances nor any funding activity were carried out by the Noticee. The Noticee relied upon its books of accounts that have been duly audited by the statutory auditors. The Committee finds that though there appear to be certain inconsistencies in the accounting relating to receipts and payments, no observations indicate that the Noticee has earned any income from the said transactions. In view of the above, Noticee's contention that it was not engaged in any fund-based activities can be accepted.
- (vi) The Noticee, however, is warned to ensure that the transactions executed by the Noticee should be supported by appropriate documentary evidence

to reflect the completeness of the transactions and henceforth follow correct accounting practices.

34.2 Utilization of client securities for purposes other than specified

- a. On verification of clients' demat accounts transactions, it was observed that ECSL had sold securities of 60 clients involving Rs.118.10 crores to recover Noticee's dues towards F&O losses of its clients, the effect of which was given by the Noticee in the respective client accounts in Register of Securities ("ROS") and financial ledgers. It was further observed that out of total securities sold by ECSL involving Rs.118.10 crores, the securities pertaining to non-related parties involving Rs.17.22 crores and securities of potential connected parties involving Rs.23.17 crores were in excess of their debit balance. These securities, valuing Rs.40.39 crores, were observed to be sold in excess of the respective client's obligations as of the date of sale of securities.
- b. In its reply to the Supplementary SCN, the Noticee submitted as under-
 - i. The Noticee relied upon its replies dated September 1, 2020, and September 29, 2020, wherein it detailed the disputes with ECSL. However, without prejudice to the same, the Noticee had replied to the specific allegations made in the Supplementary SCN.
 - ii. Out of the total 60 clients, 14 clients are related to the Noticee, and the remaining 46 clients are not related.
 - iii. There is no misuse with respect to securities sold by ECSL as the same were sold under instructions and/or to the knowledge of all concerned, except for one instance of client Rohit Kumar Jain (Client Code B06R020) involving Rs.14,685/- where the securities were sold without the knowledge of the client.
 - iv. The Noticee had duly given the credit of securities sold in the client ledger in all the non-related party clients whose securities were sold under clients' instruction/knowledge.
 - v. The fact that they had knowledge/given instructions is evident from the fact that none of the non-related party clients have raised any complaints/objections alleging the unauthorized sale of securities.
 - vi. The ledger balances considered in the Supplementary SCN are incorrect.
 - vii. The Noticee had submitted a sheet containing the correct ledger balances (including margin) and family account debit/debit balance elsewhere, which

reduces the value of securities sold from Rs.40.39 crores to Rs.9.39 crores mentioned in the show-cause notice.

- viii. Out of the total amount of Rs.9.39 crores, a sum of Rs. 6.68 crores is reduced as the clients have already submitted "No Dues" / "Complaint Withdrawal" certificates with the Exchange qua the Noticee.
- ix. Thus, the only sum due is Rs.2.71 crores, which is further adjusted towards outstanding client dues. It is pertinent to state that some non-related party clients whose securities were sold under their instructions/knowledge were having debit balances (payable to the Noticee / IndiaNivesh Group Companies) either in their family accounts or under margin or NBFC books separately.

c. The Committee finds as under:

- i. With respect to the Noticee's contention that it has relied upon the replies dated September 1, 2020, and September 29, 2020, wherein the Noticee had detailed the disputes with ECSL, the Committee finds that the same is not germane to the charges levelled in the Supplementary SCN. Any dispute between the Trading Member and the Clearing Member is a dispute inter se for which the recourse is available through the appropriate authority. The same cannot be a subject matter before this Committee. The Notice cannot take refuge in the fact that the Exchange had impleaded itself in the tripartite case of HDFC Bank, ECSL and Noticee. The Exchange impleaded in the said matter only to protect the interest of the investors, as the Exchange had till April 2020 received more than 800 investor complaints against the Noticee.
- ii. The Noticee's contention that the securities sold by ECSL were under the instructions and knowledge of all concerned, except for one client and therefore there is no misuse of client securities, is incorrect and devoid of any merit. The Noticee's contention that all known related party clients whose securities were sold were under the instructions and due credit had been given in the ledger, and there is no complaint from any one of them with respect to an unauthorized sale, is incorrect since some of the related party clients had also complained. The Noticee's contention that it had resolved any dispute/grievance with respect to such sale does not imply that there was no misuse of client securities.
- iii. The Noticee's contention that the value of the securities sold is Rs.9.39 crores and not Rs.40.39 crores is on account of considering the notional

margin against the value of such securities. However, the said contention of the Noticee is not tenable as margin entries are notional in nature and reversed on the next day. Further, the Noticee's claim that the clients had debit balance in their family accounts/elsewhere is not tenable as inter-client adjustments are prohibited. Further, although the Noticee had claimed that the sale of the securities was known to the clients, the Noticee has not provided any proof of pre-order confirmation from such clients.

- iv. The Noticee's contention that the computation of misuse indicated in Exhibit 2 of the Supplementary SCN is incorrect, as the misuse of Rs.9.39 crores is reduced to Rs.2.71 crores after considering Rs.6.68 crores towards the clients who had given no dues/complaint withdrawal certificates. The Committee, without going into the merits of the contention, *prima facie* finds that it is an admitted fact which is also borne out from the records available with the Exchange that there was a misuse. Any subsequent consents for set-off/mutual adjustments do not per se take away the observation pertaining to misuse.
- v. The Committee, therefore, finds that the Noticee's contention is devoid of any merits as the Noticee has failed to establish that there was no misuse.

FINDINGS OF MCSGFC

35. The findings of the Committee are as under:

- a. The Noticee has misused the funds of credit balance clients to meet the settlement obligation of debit balance clients resulting in a shortfall of funds of Rs.93.26 crores. The Noticee further misused the funds of credit balance clients to meet the margin obligations of debit balance clients to the tune of Rs.99.43 crores. Thus, the Noticee acted in violation of Regulation 4.5.3 (e) of NSEIL Regulations (CM and F&O Segments) and Exchange Circular No.NSE/INSP/33276 dated September 27, 2016.
- b. ECSL sold client securities worth Rs.40.39 crores as the Noticee could not fulfill its obligations. Therefore, the Noticee had misused the client securities as the client securities cannot be utilized by the Noticee for any purposes other than those specified. Thus, the Noticee acted in violation of Regulation 4.5.3 (e) of NSEIL Regulations (CM and F&O Segments).

c. The Noticee has failed to abide by the Code of Conduct specified under Regulations 4.5.1 and 4.5.2 of NSEIL Regulations (CM and F&O Segments). Some of the provisions are given below:

4.5.1 Adherence to SEBI Code of Conduct

The Trading Member shall at all times subscribe to the Code of Conduct as prescribed by the Securities and Exchange Board of India (Stock Brokers) Regulations, 1992.

4.5.2 General Principles

(a) Professionalism: A Trading Member in the conduct of his business, shall observe high standards of commercial honour of just and equitable principles of trade.

(b) Adherence to Trading Practices: Trading Members shall adhere to the Rules, Regulations and Byelaws of the Exchange and shall comply with such operational parameters, rulings, notices, guidelines and instructions of the relevant authority as may be applicable from time to time.

(c) Honesty and Fairness: In conducting his business activities, a Trading Member shall act honestly and fairly, in the best interests of his constituents.

d. The Noticee, vide its email dated January 27, 2022, has submitted that since it has already been under voluntary disablement for a substantial period, they are willing to continue voluntary disablement for a further period of upto 45 days, for the following reasons-

- i. That there are no pending investor complaints, it has settled the dues of its Clearing Member, ECSL as well as its bankers, and
- ii. Has been engaging with financial institutions to avail banking facilities and interacting with its corporate customers and HNI clients to restart its business.

e. The Noticee has further stated its revival plans will be at great peril if it is penalised with any form of suspension. The said request of the Noticee cannot be considered in absolute terms as the Committee observed the following-

- i. The Noticee had misused client assets to the tune of more than Rs.100 crores which has been discussed in detail as above. It is, therefore, a matter of record that the Noticee has completely failed to ensure that the client assets are not misused.

- ii. The prescribed penalty in case of misuse of client funds is 1% of the amount of misuse i.e., Rs.2.33 crores [1% of Rs.233.08 crores (Rs.93.26 crores + Rs.99.43 crores+ Rs.40.39 crores)] OR Rs.1 lac, whichever is higher. The Noticee has failed to have in place an appropriate risk management system and robust compliance, which has led to a situation of misuse of client assets. This has also resulted in immense stress and pain to the investors at large as many of them had to wait for more than 6 months for settlement. Therefore, the Committee is of the view that though the Noticee has subsequently taken steps to settle all the investors' claims, the fact remains that Exchange Rules relating to client assets have been violated and further there was a long period when investors had no access to their funds and securities.
- f. Exchange circular NSE/INSP/36248 dated November 06, 2017, provides for the penalty to be applied in respect of various violations as identified during the inspection of the members. This circular *inter alia* states that “....the penalties/disciplinary action(s)/charges are indicative in nature and could undergo change in specific cases depending on the frequency and gravity of the violations.....Penalty/disciplinary action in respect of violations having high impact would be dealt with on case to case basis depending on seriousness and gravity of such violations....”.The Committee further observed that the said penalty structure *inter alia* prescribes suspension in case of serious violations. The violations observed in the instant case are grave as more than Rs.100 crores of client assets were misused by the Noticee. Therefore, the Committee finds it necessary to initiate suitable disciplinary action which would act as a deterrent, in addition to monetary penalty.
- g. The Committee, however, finds that the Noticee had taken efforts to settle client dues. It is also a matter of the fact that currently there are no pending investor complaints against the Noticee. The Noticee, vide letter dated December 26, 2021, has also claimed to have complied with the net worth requirement and that its net worth is Rs.11.99 crores as on December 15, 2021.

DECISION

36. Given the facts and circumstances as well as the findings as mentioned in the preceding paragraphs, apart from the monetary penalty that is being levied in the present case, the Committee finds it appropriate that the trading membership of the Noticee be suspended

for a period of six months from the date of this order and considering the principles of proportionality, a monetary penalty of Rs.1 crore be levied for the observed violations.

37. In view of the above, the Committee imposed the following penalty as indicated against each of the violations:

| Sr. No. | Committee Findings | Penalty prescribed as per Exchange Circular Nos. NSE/INSP/36248 dated November 06, 2017 | Penalty Levied |
|---------|--|---|---|
| 1 | Funds of credit balance clients used for meeting the settlement obligations of debit balance clients resulting in a shortfall of clients' funds involving Rs.93.26 crores. | 1% of the amount involved or Rs.1 lac, whichever is higher, | Monetary penalty of Rs.1,00,00,000/- plus suspension of trading membership for a period of six months |
| 2 | Funds of credit balance clients used for meeting the meeting margin obligations of debit balance clients to the tune of Rs.99.43 crores. | 1% of the amount involved of Rs.233.08 crores (Rs.93.26 crores + Rs.99.43 crores+ Rs.40.39 crores) being Rs.2,33,08,000/- | |
| 3 | Misuse of client securities for purposes other than specified involving Rs.40.39 crores | | |
| 4 | Engagement as a principal in a business other than that of securities involving personal financial liability in case of 3 related parties involving Rs.72.19 crores | No prescribed penalty | |
| | | Total | Rs.1,00,00,000/- |

38. The Noticee shall pay the monetary penalty of Rs.1,00,00,000/- (Rupees One Crore Only).

39. The trading membership of the Noticee shall remain suspended for a period of six months from the date of this order.
40. The continuation of the membership of the Exchange post the period of suspension shall be subject to the satisfactory compliance of all the conditions prescribed for being a member of the Exchange and as in force from time to time, including maintenance of prescribed net worth during the entire period of suspension and thereafter upon assumption of operations to submit a quarterly certificate from a practicing Chartered Accountant satisfying the conditions that may be imposed by the Exchange.
41. The proceedings of the MCSGFC meeting were held on January 18, 2022, through video conferencing. At this stage, it is not possible to sign a copy of this order, nor the Exchange can issue a certified copy of the order. Therefore, an electronic copy of this order sent from the Exchange's email id shall be treated as a signed copy for all purposes.

Sd/-
Mona Bhide
(Chairperson)

Sd/-
K Narasimha Murthy
(Committee Member)

Sd/-
Vikram Limaye
(Committee Member)

Date: February 11, 2022