BEFORE THE ADJUDICATING OFFICER
SECURITIES AND EXCHANGE BOARD OF INDIA

[ADJUDICATION ORDER NO. Order/BM/DS/2024-25/30530]

UNDER SECTION 15-I OF THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992, SECTION 23-I OF THE SECURITIES CONTRACTS (REGULATION) ACT, 1956 READ WITH RULE 5 OF SEBI (PROCEDURE FOR HOLDING INQUIRY AND IMPOSING PENALTIES) RULES, 1995 AND RULE 5 OF SECURITIES CONTRACTS (REGULATION) (PROCEDURE FOR HOLDING INQUIRY AND IMPOSING PENALTIES) RULES, 2005

IN THE MATTER OF

Phillip Capital (India) Private Limited
PAN No.: **AABCR6382C**
SEBI Regn No.: INZ000169632

FACTS OF THE CASE

1. Securities and Exchange Board of India (hereinafter referred to as "**SEBI**") conducted inspection of M/s Phillip Capital (India) Private Limited (hereinafter referred to as "**Noticee/ Phillip / the Company**") from November 21, 2022 to December 03, 2022 to look into various compliance requirements adhered by the Noticee. The period covered in inspection was from April 01, 2021 to October 31, 2022 (hereinafter referred to as "**inspection period**" / "**IP**"). Noticee is registered as stock broker with SEBI registration no. INZ000169632.

2. The findings/ observations made during the course of inspection were communicated to the Noticee by SEBI vide letter dated January 12, 2023. After examining the reply submitted by the Noticee vide letters dated January 25, 2023 and October 17, 2023, it has been alleged that the Noticee violated various provisions of Securities Contracts (Regulation) Rules, 1957 (hereinafter referred

to as "**SCR Rules, 1957**") and applicable SEBI Circulars. The summary of violations alleged to have been committed by the Noticee and the corresponding provisions of SCR Rules, 1957 and SEBI Circulars are given in the table below:

<u>Table 1</u>

Sr. No.	**Alleged Violations (Summarized)**	**Regulatory Provisions**
1	Nomenclature of bank accounts not in prescribed format	Clause 1 of Annexure to SEBI Circular No. SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016
2	Incorrect reporting of enhanced supervision data (weekly) (NSE)	Clause 3 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016
3	Incorrect reporting of data regarding bank balance and cash and cash equivalent balances	Clause 3.2 of Annexure to SEBI Circular No. SEBI/HO/MIRSD/MIRSD2/CIR/P/ 2016/95 dated September 26, 2016
4	Non adherence to the rules of membership	Rule 8(3)(f) of SCR Rules, 1957
5	Improper dealing	Clause 3 of SEBI Circular SEBI/ MIRSD//Cir-06/2004 dated January 13, 2004
6	Cyber security and cyber resilience	Clause 36, 41 and 42 of Annexure 1 to the SEBI Circular SEBI/HO/MIRSD/CIR/PB /2018/147 dated December 03, 2018

3. SEBI initiated adjudication proceedings against the Noticee under Section 15A(b) and Section 15HB of SEBI Act, 1992 and Section 23H of Securities Contracts

(Regulation) Act, 1956 (hereinafter referred to as "**SC(R) Act, 1956**") for the alleged violations of the relevant provisions as stated above.

APPOINTMENT OF ADJUDICATING OFFICER

4. The undersigned was appointed as the Adjudicating Officer **(AO)** vide Order dated January 23, 2024 under Section 15-I of the SEBI Act, 1992, and Rule 3 of SEBI (Procedure for Holding Inquiry and Imposing Penalties) Rules, 1995 (hereinafter referred to as "**SEBI Adjudication Rules**") and under Section 23-I of SC(R) Act, 1956 read with and Rule 3 of Securities Contracts (Regulation) (Procedure for Holding Inquiry and Imposing Penalties) Rules, 2005 (hereinafter referred to as "**SCRA Adjudication Rules**"), to inquire into and adjudge under Section 15A(b) and Section 15HB of SEBI Act, 1992 and Section 23H of SC(R) Act, 1956, the violations of aforesaid provisions alleged to have been committed by the Noticee.

SHOW CAUSE NOTICE, REPLY OF THE NOTICEE AND HEARING

5. Show Cause Notice No. SEBI/EAD/BM/DS/12394/1/2024 dated March 27, 2024 (hereinafter referred to as **"SCN"**) was issued to the Noticee in terms of Section 15-I of the SEBI Act, 1992 and rule 4 of SEBI Adjudication Rules and Rule 4 of SCRA Adjudication Rules, 2005 read with section 23-I of SC(R) Act, 1956, to show cause as to why an inquiry should not be held against it and why penalty, if any, under Section 15A(b) and Section 15HB of SEBI Act, 1992 and Section 23H of SC(R) Act, 1956 be not imposed on the Noticee.

6. The SCN was duly served on the Noticee through SPAD and digitally signed e-mail. The Noticee submitted its reply to the SCN vide letter dated May 03, 2024.

7. The submissions made by the Noticee are as summarized below:

7.1. <u>Nomenclature of bank accounts not in prescribed format</u>

7.1.1. Noticee has submitted that bank accounts are maintained with correct nomenclature with the Client account tagging. Further, it has taken letters from the banks to show that the nomenclature of the account was with the client tagging, which have been submitted in support of its submissions.

7.1.2. Following are the details of client tagging as per letters provided by banks.

<u>Table - 2</u>

Sr. No.	*Bank Account No.*	*Account Name*	*Name as per letter from bank*
1	*SCB-A/C No. 22205548225*	*PHILLIPCAPITAL (INDIA) PVT LTD*	*Trade ON Go PCI **Client Account***
2	*ICICI Bank A/c No. 405117510*	*PHILLIPCAPTIAL (INDIA) PRIVATE LIMITED-MCX*	*PHILLIPCAPITAL(INDIA) PRIVATE LIMITED.-MCX COMMODITY **CLIENT ACCOUNT***

7.2. <u>Incorrect reporting of enhance supervision data (Weekly) (NSE)</u>

7.2.1. The bank balance in client accounts and Noticee's settlement account and collaterals maintained with the exchanges is always much greater than the funds provided by the Clients. Even as per the NSE workings for all the weeks that NSE had inspected, the Noticee had excess funds ranging from ₹ 62 crores to ₹ 151 crores.

7.2.2. The intention of Enhance Supervision reporting is to find out mis-utilisation of client funds and from the working provided by the Exchange also it is evident that there is no mis-utilisation by the Noticee, as it has much higher excess funds with itself at all points of time.

7.2.3. On April 05, 2022, NSE Offsite Inspection team issued a Letter of Observation in "Cash and Cash Equivalent" reporting done by the

Noticee for the period Oct 2021 to Feb 2022. The Noticee has already been penalized by NSE. Hence, Noticee requested not to charge it again on same instance again as a principle of natural justice. Necessary changes have already been done in its back office system with effect from 11.04.2022 after taking into consideration above points.

7.2.4. The Noticee has also provided detailed response (which is stated and dealt in the forthcoming paragraphs)

7.3. Incorrect reporting of data regarding bank balance and cash and cash equivalent balances

7.3.1. With respect to the allegation of submission of incorrect data regarding bank balances, the Noticee submitted that it had correctly submitted the weekly data. The difference was only in few bank accounts and mainly on account of un-cleared cheques. The clear balance has to be manually calculated from the bank statement and there was an inadvertent error occurred while calculating the same. The instance wise reply was also provided by the Noticee.

7.3.2. With respect to the allegation of submission of incorrect data regarding Cash and Cash Equivalent (C&CE) balances – Noticee submitted the following reasons.

7.3.2.1. Mismatch in reporting due to software issue –

7.3.2.1.1. T-day derivative bill for MTM and Delivery were not considered while reporting Financial Ledger (clear) in C&CE reporting.

7.3.2.1.2. There was technical bug in software on account of which Funds received in margin ledger on T day and transaction in BSE star segment were not considered while reporting Financial Ledger (clear) in C & CE.

7.3.2.1.3. In this regard, the Noticee has stated that on April 5, 2022, NSE Offsite Inspection team had issued a Letter of Observation in "Cash and Cash Equivalent" reporting done by the Noticee for Oct 2021 to Feb 2022. The Noticee has already been penalised for the same by the NSE. Hence, it should not be penalised again for the same instances. Further, necessary changes have already been done in its back office system and with effect from 11.04.22 after taking into consideration above points.

7.3.2.2. There are various aspect in Cash and Cash Equivalent (C&CE) which are not required to be reported and "Not mentioned in Trial balance"

7.3.2.2.1. As per NSE circular no. NSE/INSP/44478 dated 27th May 2020 custody settled clients are not required to be reported in C&CE reporting. Accordingly, the Noticee has not reported the same. Hence this difference should not be considered.

7.3.2.2.2. Client accounts against which the Noticee has made a provision has not been considered while reporting Financial Ledger (clear) in C&CE.

7.3.2.2.3. Error accounts which are proprietary in nature are not required to be reported in while reporting Financial Ledger (clear) in C & CE.

7.3.2.2.4. In few instances MTF and non-MTF balances have been consolidated while reporting Financial Ledger (clear) in C&CE.

7.3.2.3. The Noticee has provided instance wise reply.

7.4. <u>Non Adherence of the rules of Membership</u> –

7.4.1. The Noticee has a Net-worth of Rs. 431 crores as on March 31, 2022. The net-worth requirement for a clearing member is Rs. 10 crores. Thus, it has a significantly higher net-worth than the requirement. During the financial year and after adjusting inter corporate deposit; the Noticee still had significantly excess net-worth than the regulatory requirement. Even maximum amount of inter corporate deposit at any given point of time is approx. Rs.100 crores. Hence, at any given point of time, the Noticee had 300% excess funds available in the Company.

7.4.2. The inter-company deposits were given as highlighted in the Notice is cumulative for the entire financial year. Hence considering the cumulative amount is not giving the correct picture. Further there is no financial liability on PhillipCapital by giving such inter-corporate deposit. Eg. If on day one we have given 10 crores and taken it back on day 2. On day 4 we have given 20 crores and taken it back on day 5 on day 7 we have given 15 crores and taken it back on day 9. Then in the above situation the notice has considered the cumulative amount of 10+20+15 i.e 45 crores. The above is not giving correct picture since at any point of time that net outstanding did not cross 20 crores.

7.4.3. The inter-company deposits were advanced from its proprietary bank accounts and there is no observation that the client funds were utilized to provide inter-company deposit. The inter-company deposits were made as a temporary investment of surplus funds similar to investment in liquid funds with a bank or mutual fund purely to earn interest on available surplus funds.

7.4.4. SEBI's circular dated May 7, 1997 clarified that borrowing and lending funds by a trading member, in connection with or incidental to or consequential upon the securities business would not disqualify a trading *member under Rule 8(3)(f) of the SCR Rules. Investment of surplus funds, generated as a consequence of securities business, with a group company cannot lead to an inference that the company is engaged as a principal in business other than that of securities involving personal financial liability.*

7.4.5. Noticee further submitted that the entities to whom the loans were given were its subsidiaries or group companies, and inter-corporate deposits were given for their working capital requirements. This also includes intraday advance given by the company. Deposits were given from own funds of the company and for temporary period i.e. 3 to 5 days and have been since been repaid.

7.5. <u>Improper dealing</u> - Trading through Sushil Financial Services Private Limited (NSE TM code – 06074) and CNB Finwiz Private Limited (TM code – 11893) is purely a PMS activity. Inspecting official had misconstrued the same as a regular activity of proprietary trading or trading on behalf of clients. Further, the Noticee has received clarification from NSE also, that prior approval from the Exchange is not required for trading through other members solely for the purpose of PMS transactions and said clarification is in line with SEBI circular ref. no. SEBI/HO/IMD/DF1/CIR/P/2020/26 dated February 13, 2020. Noticee has submitted a copy of the email clarification received from the NSE. Thus, the Noticee has complied with Exchange and SEBI guidelines.

7.6. <u>Cyber Security and Cyber resilience</u> –

7.6.1. Noticee is using Exchange empaneled vendors software. It has requested STQC certification from Vendors, and they have given confirmation/ self-certification with respect to compliance with SEBI circular on Cyber Security instead of STQC certificate. Further, it is an industry wide issue. The Noticee is only using vendors approved by the *exchange. The Noticee has done the VAPT during the Inspection period details are as follows.*

SN	*Financial Year*	*Date of VAPT*
1	*2021-2022*	*March 25, 2022*
2	*2022-2023*	*September 15, 2022*

7.6.2. As per regulation VAPT is required to be done once in a financial year, which has been adhered to by the Noticee. It has submitted screenshots / evidence of the VAPT done and submissions made.

8. Vide letter dated May 22, 2024, hearing notice was issued to the Noticee to provide opportunity of personal hearing in the interest of natural justice. The Noticee was advised to appear before the undersigned on June 18, 2024. The Noticee appeared for the scheduled hearing through its authorized representative (**AR**). The AR reiterated submissions already made vide letter dated May 03, 2024 and also made additional submissions during the course of the hearing. The AR requested for time till June 21, 2024 to submit the additional submissions in writing, which was granted by the undersigned. The additional submissions made by the Noticee vide letter dated June 21, 2024 are as summarized below.

8.1. The Noticee submitted copies of the cheque of its two bank accounts in support of its submission that the nomenclature was correct and is correctly reflected on the face of the cheques.

8.2. With respect to incorrect reporting of enhanced supervision data, the Noticee submitted that the process was manual, with dependency on the exchanges and the clearing corporation, and during the inspection period, which coincided with the covid period, the Noticee's staff was working from home. The errors were purely human errors. Since January, 2024, the reporting has been discontinued by the Exchanges.

8.3. EOD Balance in all Client Bank Accounts - Noticee submitted a copy of the bank statement to demonstrate how the clear balance is arrived, by excluding the uncleared balances manually, which makes it more prone to human errors, which have occurred in the present case.

8.4. Collateral deposited with Exchanges in the form of Cash and Cash Equivalents - The files provided by the exchanges were to be manually inputted to calculate the total collaterals deposited with the exchanges. The issue was mainly on account of MSEI exchange – where since it is an inactive segment, the collaterals details were not obtained on a daily basis and the balances were accordingly not updated. It was also a human error.

8.5. Total Credit Balance of all clients and Total debit Balance of all clients - The error was not in segregation reporting but the client balances which were reported as part of Cash & Cash Equivalent reporting. The Noticee has already been penalized for the same by the NSE. In support of its submissions, a letter received from the NSE has been submitted by the Noticee.

8.6. Non adherence to rules of Membership – Inter-corporate deposits (ICDs) were given to the associate / group companies out of their owned funds, at arms length, and reasonable interest was charged from the companies. Noticee also submitted TDS certificate in support of its submissions. As abundant caution, the Noticee has stopped giving ICDs after clarification issued by the NSE.

8.7. Improper dealing – Noticee had opened the trading account with other broker only for the portfolio management license. The Noticee has also submitted email confirmation received from Sushil Financial Services Private Limited, confirming that its accounts were opened under PMS category. In any case, even when the Noticee was not required to seek approval from the NSE, as clarified by the NSE itself, the Noticee has never placed trades with both the brokers at any point of time. The last trade date with CNB Finwiz Private

Limited was January 12, 2022 and the first trade date with Sushil Financial Services Private Limited was January 17, 2022.

8.8. *Cyber security and resilience – With respect to query during the hearing as to why were the VAPT certificates were not submitted by the Noticee during the inspection, the Noticee has submitted that in the observation issued by the SEBI on January 12, 2023, there was no observation with respect to VAPT audit.*

8.9. *With respect to STQC, the Noticee only uses exchange empaneled vendors for its front office and back office operations. These vendors do not provide STQC certificate at present, and this is a system wide issue, with all the brokers.*

CONSIDERATION OF ISSUES AND FINDINGS

9. Considering the allegations made out in the SCN and the submissions made by the Noticee, I find that following issues require consideration in the present case:

   ISSUE I - Whether the Noticee is in violation of the provisions of SCR Rules, 1957 and applicable SEBI Circulars, as given in Table 1 above?

   ISSUE II - Do the violations, if any, attract penalty under Section 15A(b) and Section 15HB of the SEBI Act, 1992 and Section 23H of SC(R) Act, 1956?

   ISSUE III - If so, what would be the monetary penalty that can be imposed taking into consideration the factors mentioned in Section 15J of SEBI Act, 1992 and Section 23J of SC(R) Act, 1956?

10. The said provisions under which violations have been alleged against the Noticee are reproduced below –

    Securities Contracts (Regulation) Rules, 1957

    Qualifications for membership of a recognised stock exchange

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

(1)…

(2)…

(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—

(a)…

(b)…

(c)…

(d)…

(e)…

(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, provided that—

(i)the governing body may, for reasons, to be recorded in writing, permit a member to engage himself as principal or employee in any such business, if the member in question ceases to carry on business on the stock exchange either as an individual or as a partner in a firm,

(ii)in the case of those members who were under the rules in force at the time of such application permitted to engage in any such business and were actually so engaged on the date of such application, a period of three years from the date of the grant of recognition shall be allowed for severing their connection with any such business,

(iii)nothing herein shall affect members of a recognised stock exchange which are corporations, bodies corporate,

companies or institutions referred to in items (a) to (n)of sub-rule (8).

SEBI Circular No. SEBI/MIRSD//Cir-06/2004 dated January 13, 2004 - Review of norms relating to trading by members/sub brokers.

3. With a view to address these concerns, stock exchanges are directed to ensure the following:-

3.1 A stock broker/ sub broker of an exchange cannot deal with brokers/sub brokers of the same exchange either for proprietary trading or for trading on behalf of clients, except with the prior permission of the exchange. The stock exchanges while giving such permission, shall consider the reasons stated by the brokers/sub brokers for dealing with brokers/sub brokers of the same exchange and after carrying out due diligence allow such brokers/sub brokers to deal with only one stock broker/sub broker of the same exchange.

3.2 A stock broker/sub broker of an exchange can deal with only one broker/sub broker of another exchange for proprietary trading after intimating the names of such stock broker/sub broker to his parent stock exchange.

3.3 As per Regulation 15(1) (e) of the SEBI (Stock Brokers and Sub Brokers)Regulations, 1992 a sub-broker shall not be affiliated to more than one stockbroker of one stock exchange. It is reiterated that a stock broker of an exchange can deal with only one broker of another exchange on behalf of clients after obtaining necessary registration as a sub broker.

SEBI Circular No. SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016 - Enhanced Supervision of Stock Brokers/Depository Participants

<u>Annexure</u>

1.Naming / Tagging of Bank and Demat Accounts by Stock Broker

1.1.Bank accounts and Demat accounts maintained by all stock brokers shall have appropriate nomenclature to reflect the purpose for which those bank/demat accounts are being maintained.

1.2.The nomenclature for bank accounts and demat accounts to be followed is given as under:

1.2.1.Bank account(s) which hold clients funds shall be named as "Name of Stock Broker -Client Account".

1.2.2.Bank account(s) which hold own funds of the stock broker shall be named as "Name of Stock Broker -Proprietary Account".

1.2.3.Demat account(s)which hold clients' securities shall be named as "Name of Stock Broker-Client Account".

1.2.4.Demat account(s), which hold own securities of the stock broker, shall be named as "Name of Stock Broker-Proprietary Account".

1.2.5.Demat account(s), maintained by the stock broker for depositing securities collateral with the clearing corporation, shall be named as "Name of Stock Broker-Collateral Account".

1.2.6.Demat account(s) held for the purpose of settlement would be named as " Name of Stock Broker -Pool account".

1.2.7.Bank account(s) held for the purpose of settlement would be named as " Name of Stock Broker -Settlement Account"

3. Monitoring of Clients' Funds lying with the Stock Broker by the Stock Exchanges

3.1. Stock Exchanges shall put in place a mechanism for monitoring clients' funds lying with the stock broker to generate alerts on any misuse of clients' funds by stock brokers, as per the guidelines stipulated in para 3.2 & 3.3 below.

3.2. Stock brokers shall submit the following data as on last trading day of every week to the Stock Exchanges on or before the next trading day:

A- Aggregate of fund balances available in all Client Bank Accounts, including the Settlement Account, maintained by the stock broker across stock exchanges

B- Aggregate value of collateral deposited with clearing corporations and/or clearing member (in cases where the trades are settled through clearing member) in form of Cash and Cash Equivalents (Fixed deposit (FD), Bank guarantee (BG), etc.) (across Stock Exchanges). Only funded portion of the BG, i. e. the amount deposited by stock broker with the bank to obtain the BG, shall be considered as part of B.

C- Aggregate value of Credit Balances of all clients as obtained from trial balance across Stock Exchanges (after adjusting for open bills of clients, uncleared cheques deposited by clients and uncleared cheques issued to clients and the margin obligations)

D- Aggregate value of Debit Balances of all clients as obtained from trial balance across Stock Exchanges (after adjusting for open bills of clients, uncleared cheques deposited by clients, uncleared cheques issued to clients and the margin obligations)

E- Aggregate value of proprietary non-cash collaterals i.e. securities which have been deposited with the clearing corporations and/or clearing member (across Stock Exchanges)

F- Aggregate value of Non-funded part of the BG across Stock Exchanges

P - Aggregate value of Proprietary Margin Obligation across Stock Exchanges

MC - Aggregate value of Margin utilized for positions of Credit Balance Clients across Stock Exchanges

MF- Aggregate value of Unutilized collateral lying with the clearing corporations and/or clearing member across Stock Exchanges

3.3.Based on the aforesaid information submitted by the stock broker, Stock Exchanges shall put in place a mechanism for monitoring of clients' funds lying with the stock brokers on the principles enumerated below:

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

Principle:

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

Stock Exchanges shall calculate the difference i.e. G as follows –

G = (A+B)-C

If difference G is negative, then the total available fund is less than the ledger credit balance of clients. The value of Gmay indicate utilization of clients' funds for other purposes i.e. funds of credit balance clients are being utilized either for settlement obligations of debit balance clients or for the stock brokers' own purposes. The negative value of G acts as an alert to the Stock Exchanges.

Thereafter, the absolute value of G shall be compared with debit balance of all clients as per client ledger D as follows:

If the absolute value of (G) is lesser than |D|, then the stock broker has possibly utilised funds of credit balance clients towards settlement obligations of debit balance clients to the extent of value of G.

If the absolute value of (G) is greater than |D|, then the stock broker has possibly utilised a part of funds of credit balance clients towards settlement obligations of debit balance clients and remaining part for his own purposes. In such cases the amount of client funds used for own purpose is calculated as follows:

$H = |G| - |D|$

3.3.2.Funds of clients used for Margin obligation of proprietary trading:

Stock Exchanges shall thereafter, verify whether the proprietary margin obligations (across Stock Exchanges) is less than the own funds and securities lying with the Stock Exchanges as collateral deposit, as follows:

Principle:

The sum of Proprietary funds and securities i.e. (G + E + F) lying with the clearing corporation/clearing member should be greater than or equal to Proprietary margin obligations (P)

If value of G is positive (i.e. A+B > C), then proprietary funds are lying with the clearing corporation/clearing member and/or client bank accounts along with the clients funds to the extent of positive value of G.

The sum of the proprietary funds (positive value of G), the value of proprietary securities (E) and the non-funded portion of bank guarantee (F) available in the Stock Exchanges is compared with the Proprietary margin obligations (P).

If P > (G+E+F), then Stock Exchange shall calculate the difference I, which is the amount of proprietary margin obligation funded from clients assets.

I = P -(G+E+F)

If G is negative, then, value of G is considered as 0, as there is no proprietary funds lying with the stock exchange.

The value of I indicates the extent of funds and securities of clients which is possibly utilised towards proprietary margin obligations. This value of I acts as an alert to the Stock Exchanges on the possible mis-utilisation of clients' assets towards proprietary margin obligations.

3.3.3.Funds of credit balance clients used for Margin obligations of debit balance clients and proprietary trading:

Stock Exchanges shall thereafter, verify whether the clients funds lying with the clearing corporation/clearing member are utilised towards margin obligations of debit balance clients and proprietary margin obligations.

Principle:

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)

If value of G is positive (i.e. A+B > C), then fund lying with the clearing corporation/clearing member (B) may contain proprietary and clients' fund. Hence, the value of clients funds lying with the clearing corporation/ clearing member i.e. (C-A)shall be considered in the place of B.

In such cases, (C-A)is compared with Margin obligations of credit balance clients and the free deposits available with the clearing corporation/clearing member. The value of J, which is clients' funds utilised towards margin obligations of debit balance clients and proprietary margin obligations, is calculated as under:

J = (C -A) -(MC + MF)

The value of J, if positive, indicates the extent of clients' funds utilised 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 mis-utilisation of clients' funds towards margin obligations of debit balance clients and proprietary margin obligations.*

3.4.Based on the alerts generated, Stock Exchange shall, inter-alia, seek clarifications, carry out inspections and initiate appropriate actions to protect the clients' funds from being misused. Stock Exchanges shall also maintain records of such clarifications sought and details of such inspections. The aforesaid calculations are illustrated in tabular format in Table 1, 2 & 3 given at the end of the annexure.

3.5.Stock Exchanges shall put in place the aforesaid monitoring mechanism within three months from the date of this circular and carry out the monitoring of clients' funds for all stock brokers, except for those who are carrying out only proprietary trading and/or only trading for institutional clients.

3.6.Stock Brokers shall ensure due compliance in submitting the information to the Exchanges within the stipulated time.

SEBI Circular No. SEBI/HO/MIRSD/CIR/PB/2018/147 dated December 03, 2018 - Cyber Security & Cyber Resilience framework for Stock Brokers / Depository Participants

Certification of off-the-shelf products

36.Stock Brokers / Depository Participants should ensure that off the shelf products being used for core business functionality (such as Back office applications) should bear Indian Common criteria certification of Evaluation Assurance Level 4. The Common criteria certification in India is being provided by (STQC) Standardisation Testing and Quality Certification (Ministry of Electronics and Information Technology). Custom developed / in-house software and components need not *obtain the certification, but have to undergo intensive regression testing, configuration testing etc. The scope of tests should include business logic and security controls.*

<u>Vulnerability Assessment and Penetration Testing (VAPT)</u>

41.Stock Brokers / Depository Participants should regularly conduct vulnerability assessment to detect security vulnerabilities in their IT environments exposed to the internet.

42.Stock Brokers / Depository Participants with systems publicly available over the internet should also carry out penetration tests, at-least once a year, in order to conduct an in-depth evaluation of the security posture of the system through simulations of actual attacks on its systems and networks that are exposed to the internet. In addition, Stock Brokers / Depository Participants should perform vulnerability scanning and conduct penetration testing prior to the commissioning of a new system that is accessible over the internet.

11. I will now proceed with my findings in each of the alleged violations against the Noticee in the SCN dated March 27, 2024.

12. <u>Nomenclature of bank accounts not in prescribed format</u>

12.1. It was observed that nomenclature of two out of the 24 bank accounts, client account tagging was missing from the account name. The details are provided in the table below.

Sr. No.	Bank Account No.	Account Name
1	SCB-A/C No. 22205548225	PHILLIPCAPITAL (INDIA) PVT LTD

Sr. No.	Bank Account No.	Account Name
2	ICICI Bank A/c No. 405117510	PHILLIPCAPTIAL (INDIA) PRIVATE LIMITED-MCX

12.2. As per Clause 1 of Annexure to SEBI Circular No. SEBI/HO/MIRSD/MIRSD2/ CIR/P/2016/95 dated September 26, 2016, bank accounts which hold clients' funds are required to be named following the *"Name of Stock Broker -Client Account"* convention.

12.3. In this regard, the Noticee has submitted bank confirmations and copies of its cheques, to demonstrate that it had opened the account using the correct nomenclature.

12.4. I note that the bank confirmations have confirmed the the following.

12.4.1. SCB-A/C No. 22205548225 was named as "TRADE ON GO PCI CLIENT ACCOUNT".

12.4.2. ICICI Bank A/c No. 405117510 was named as "PHILLIPCAPITAL (INDIA) PRIVATE LIMITED.-MCX COMMODITY CLIENT ACCOUNT".

12.5. The same is also confirmed from the copies of the cheques which the Noticee had shared in its additional submissions

12.6. In view of the aforesaid, I find that the tagging was not missing from the bank account names and the required naming convention has been followed by the Noticee. Thus, the allegation against the Noticee of violating the provisions of Clause 1 of Annexure to SEBI Circular No. SEBI/HO/MIRSD/MIRSD2/ CIR/P/2016/95 dated September 26, 2016 does not stand established.

13. Incorrect reporting of enhanced supervision data (weekly) (NSE)

13.1. It was observed from the weekly enhanced supervision data submitted to the exchanges for the weeks ended August 20, 2021, August 27, 2021, March 17, 2022, March 25, 2022, October 28, 2022, that the Noticee had allegedly incorrectly reported the data towards weekly monitoring of client funds for Total of day end balance in all Client Bank Accounts, Collateral deposited with exchanges in form of Cash and Cash Equivalents, Total Credit Balance of all clients, Total Debit balance of all clients, Proprietary margin Obligation, Margin utilized for positions of Credit Balance Clients, and Free/unblocked Collateral deposited with Clearing corporation. Thus, it was alleged that the Noticee has violated the provisions of Clause 3 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/ CIR/P/2016/95 dated September 26, 2016.

13.2. As per Clause 3 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/ CIR/P/2016/95 dated September 26, 2016, a stock broker is required to submit data for monitoring clients' funds lying with it, to the stock exchanges, as prescribed in sub-clause 3.2 of the aforesaid Annexure. The stock broker shall ensure due compliance in submitting the information to the Exchanges within the stipulated time.

13.3. The alleged incorrect details submitted by the Noticee, along with the response of the Noticee in this regard is as given below.

13.4. A - Total of day end balance in all Client Bank Accounts (In ₹)

	Submitted by the Noticee (A)	**As per Inspection Team (B)**	**Difference (A-B)**
August 20, 2021	709353174	707689143.1	1664030.92
August 27, 2021	293014637	289864503.2	3150133.8
March 17, 2022	580024108	579428658.7	595449.26
March 25, 2022	521173188	521228739.3	-55551.26

October 28, 2022	545277055	587383730.3	-42106675.29

13.4.1. In this regard, the Noticee submitted that the differences in the above instances were mainly due to uncleared cheques, which were due to an inadvertent error, as the clear balances are required to be calculated manually. With respect to October 28, 2022, the Noticee also submitted that the actual difference is of ₹14,91,226 and not of ₹ 42106675.29, as calculated by the inspection team.

13.4.2. I note that the Noticee has admitted the differences in the figures submitted by the Noticee to the Exchanges and the figures computed by the inspection team was due to error on the part of the Noticee. Therefore, I find that the Noticee has admittedly submitted incorrect figures to the Exchanges for the weekly enhanced supervision data.

13.5. <u>B - Collateral deposited with exchanges in form of Cash and Cash Equivalents (In ₹)</u>

	Submitted by the Noticee (A)	**As per Inspection Team (B)**	**Difference (A-B)**
August 20, 2021	7585719317	7580119317	5600000.33
August 27, 2021	7365050439	7359450439	5599999.83
March 17, 2022	7937950747	7907350747	30599999.56
March 25, 2022	7917885945	7932285945	-14399999.94
October 28, 2022	7449450110	6956506971	492943139.1

13.5.1. In this regard, the Noticee submitted that the files provided by the exchanges were to be manually inputted to calculate the total collaterals deposited with the exchanges. The difference of ₹ 56 lakh was mainly on account of MSEI exchange – where since it is an inactive segment, the collaterals details were not obtained on a daily basis and the balances were accordingly not updated. It was also a human error. With respect to the figures submitted on March 17, 2022, the figures for MCX were wrongly punches as ₹5,00,00,000 instead of ₹50,00,000.

13.5.2. I note that the Noticee has admitted the differences in the figures submitted by the Noticee to the Exchanges and the figures computed by the inspection team was due to inadvertent error on the part of the Noticee. Therefore, I find that the Noticee has submitted incorrect figures to the Exchanges for the weekly enhanced supervision data.

13.6. C - Total Credit Balance of all clients (In ₹) and D - Total debit balance of all clients (In ₹)

C - Total Credit Balance of all clients (In ₹)	Submitted by the Noticee (A)	As per Inspection Team (B)	Difference (A-B)
August 20, 2021	7263065581	6957939933	305125647.9
August 27, 2021	6782815538	7023038567	-240223029.4
March 17, 2022	7095605361	7312740330	-217134969.2
March 25, 2022	7118911664	7333084137	-214172472.7
October 28, 2022	5515438880	6033449500	-518010620.2

D - Total debit balance of all clients (In ₹)	Submitted by the Noticee (A)	As per Inspection Team (B)	Difference (A-B)
August 20, 2021	901413704	1019160702	-117746998
August 27, 2021	946752662	804559351.7	142193310.3
March 17, 2022	754399053	639747331.7	114651721.3
March 25, 2022	943616156	707724895	235891261
October 28, 2022	786075981	583255433	202820548

13.6.1. The Noticee has submitted consolidated reply for the allegation of incorrect reporting of total credit and debit balances of all clients. It has submitted that the differences can be categorized into two parts, which are summarized below.

13.6.1.1. Part 1 – Mismatch in reporting due to software issues – Due to software issues, T day derivative bill for MTM and Delivery were not considered while reporting Financial Ledger (clear) in Cash and Cash Equivalents Reporting (C&CE). Also, funds received in margin ledger on T-day and transaction in BSE star segment were not considered while reporting Financial Ledger (clear) in C&CE. The Noticee further submitted that the NSE has already issued a letter of observation dated April 05, 2022 and penalised the Noticee for the same errors. These errors have been rectified by the Noticee with effect from April 11, 2022. Therefore, the Noticee should not be penalized for the instances as per principles of natural justice.

13.6.1.2. Part 2 – There are various aspects of C&CE which are not required to be reported and not mentioned in the trial balance. These are summarized below.

13.6.1.2.1. Custody settled accounts are not required to be reported in C&CE as per NSE Circular NSE/INSP/44478 dated May 27, 2020.

13.6.1.2.2. Client accounts against which Bad debt provisions have been made, are not required to be reported for Financial Ledger (clear) C&CE.

13.6.1.2.3. Error accounts are proprietary in nature and are not required to be reported for Financial Ledger (clear) C&CE.

13.6.1.2.4. In few instances, margin trading Facility (MTF) and non-MTF balances have been consolidated while reporting Financial Ledger (clear) C&CE.

13.6.2. I note that the Noticee has admitted the incorrect reporting to the Exchanges and submitted that they were due to software issues and some other aspects.

13.6.3. With respect to the other aspects, I note that custody settled accounts are not required to be reported in terms of NSE Circular NSE/INSP/44478 dated May 27, 2020, only where the Noticee only does proprietary trading or all the clients are institutional clients / custody settled. However, the Noticee was also having retail clients . Thus, it was required to report these balances. With respect to error accounts, the Noticee's submissions are acceptable. With respect to client accounts with bad debt provisions, I note that such accounts are not allowed to be excluded as per the reporting provisions. Only when such balances are written off from the books of accounts, they are to be excluded from the calculation of all debit balance clients. However, the Noticee has submitted that it has made provisions for these accounts, i.e. they are not fully written off. Thus, the same should have been included by the Noticee.

13.6.4. With respect to Noticee's submission that it has already been penalized by the NSE for incorrect reporting of Financial Ledger (clear) in C&CE. I note that Noticee was penalized towards incorrect data reported towards weekly client level cash and cash equivalent balances by the NSE vide orders dated November 04, 2022 and January 09, 2023 for the instances occurred in various dates from January 07, 2021 to December 31, 2021. However, the present allegation also pertains to incorrect reporting on March 17, 2022, March 25, 2022 and October 28, 2022. Thus, the period is not same. Further, the penalty has been imposed only for instances observed in various dates from January 07, 2021 to December 31, 2021. I also note that the differences observed by the NSE were on account of software issues. However, in the present case, it is observed that there were various other reasons due to which there was incorrect reporting to the Exchanges. Therefore, Noticee's contention that it has already been penalized by the NSE, and should not be penalized again, is not acceptable.

13.6.5. Therefore, I find that the Noticee has submitted incorrect figures to the Exchanges as detailed above.

13.7. E - Proprietary margin Obligation (In ₹)

	Submitted by the Noticee (A)	**As per Inspection Team (B)**	**Difference (A-B)**
August 20, 2021	754767	2085887.37	-1331120.37
August 27, 2021	2632184	1949117.21	683066.79
March 25, 2022	2165134	2216323.54	-51189.54

13.7.1. In this regard, the Noticee submitted that it does not engage in proprietary trading. However, erroneously, the margin provided for some of the error accounts was not considered while reporting the figures. It also submitted that it has now changed the process, and such errors will not recur.

13.7.2. I note that the Noticee has admitted the differences in the figures submitted by the Noticee to the Exchanges and the figures computed by the inspection team was due to error on the part of the Noticee. Therefore, I find that the Noticee has submitted incorrect figures to the Exchanges for the weekly enhanced supervision data.

13.8. F - Value of Non funded portion of the Bank Guarantee (In Rs.)

	Submitted by the Noticee (A)	As per Inspection Team (B)	Difference (A-B)
October 28, 2022	2431500000	2171500000	260000000

13.8.1. With respect to the large difference on October 28, 2022, the Noticee has submitted that the collaterals provided to the MCX have not been considered by the inspection team, due to which the BGs are not included in their calculations. I note that the Noticee has not submitted any documents in support of its submissions. Thus, Noticee's contention is not acceptable.

13.9. MC - Margin utilized for positions of Credit Balance Clients (In ₹)

	Submitted by the Noticee (A)	As per Inspection Team (B)	Difference (A-B)
August 20, 2021	11601253892	4157496872	7443757020
August 27, 2021	8989303343	3519031504	5470271839
March 17, 2022	1857300429	4911248501.65	-3053948072.65
March 25, 2022	3206040090	1806452587	1399587503
October 28, 2022	2447308558	1500749469.10	946559088.90

13.9.1. In this regard, the Noticee has submitted the following.

13.9.1.1. For August 20, 2021 and August 27, 2021, the Noticee has correctly not deducted the value of securities / commodities repledged with CC / CM, after considering the NSE Circular NSE/INSP/50012 dated October 19, 2021.

13.9.1.2. For March 17, 2022, due to human error, client margin balances were not correctly considered.

13.9.1.3. For March 25, 2022, the inspecting officials have not captured correct margin obligations of trading members / FPI clearing through the Noticee. Further, mismatches are due to differences in total credit and debit balances (C and D).

13.9.1.4. For October 28, 2022, the inspecting officials have not captured correct margin obligations of trading members / FPI clearing through the Noticee.

13.9.1.5. With respect to the Noticee's submissions, I note the following.

13.9.1.6. I note from the computation of the MC that the value of securities / commodities repledged with CC / CM have not been deducted by the inspecting officials for August 20, 2021 and August 27, 2021. Therefore, the Noticee's submission in this regard cannot be accepted.

13.9.1.7. The Noticee had not provided the data for October 28, 2022 with respect to margin obligations of trading members / FPI clearing through the Noticee. Thus, the same was not considered by the inspecting officials.

13.9.1.8. The Noticee has admitted the differences on account of human errors and mismatches due to difference in total credit and debit balances of all clients.

13.9.1.9. Therefore, I find that the Noticee has submitted incorrect figures to the Exchanges for the weekly enhanced supervision data.

13.10. MF - Free / unblocked Collateral deposited with Clearing corporation (In ₹)

	Submitted by the Noticee (A)	**As per Inspection Team (B)**	**Difference (A-B)**
August 20, 2021	3872298600	3845401725	26896874.81
August 27, 2021	5896462701	5752624410	143838290.7
March 17, 2022	7239437990	7121562686	117875303.6
March 25, 2022	6403265934	7046965934	-643699999.8
October 28, 2022	6920086290	5675668205.36	1244418084.64

13.10.1. The Noticee has submitted the following.

13.10.1.1. August 20, 2021 and August 27, 2021 – The difference is only of ₹56 lakh due to inadvertent error in manual population of the file provided by the clearing corporation. The other difference are due to not consideration of the correct balances by the inspecting offiicials.

13.10.1.2. Remaining three instances - The difference is only of ₹63 lakh due to inadvertent error in manual population of the file provided by the clearing corporation. The other differences are due to not consideration of the correct balances by the inspecting offiicials.

13.10.2. I note that the Noticee has admitted the differences in the figures submitted by the Noticee to the Exchanges and the figures computed by the inspection team was due to error on the part of the Noticee. Therefore, I find that the Noticee has submitted incorrect figures to the Exchanges for the weekly enhanced supervision data.

13.11. In view of the foregoing sub-paragraphs, I find that the Noticee had incorrectly reported the data towards weekly monitoring of client funds for Total of day end balance in all Client Bank Accounts, Collateral deposited with exchanges in form of Cash and Cash Equivalents, Total Credit Balance of all clients, Total Debit balance of all clients, Proprietary margin Obligation, Margin utilized for positions of Credit Balance Clients, and Free/unblocked Collateral deposited with Clearing corporation, and thus, it has violated the provisions of Clause 3 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/ CIR/P/2016/95 dated September 26, 2016.

14. Incorrect reporting of data regarding bank balance and cash and cash equivalent balances

14.1. It was alleged that the Noticee had incorrectly submitted data regarding bank balances and client level cash and cash equivalents balances for the weeks ended on August 20, 2021, August 27, 2021, March 17, 2022, March 25, 2022, October 28, 2022, and has thereby, violated the provisions of Clause 3.2 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/ CIR/P/2016/95 dated September 26, 2016.

14.2. As per Clause 3.2 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/ CIR/P/2016/95 dated September 26, 2016, a stock broker is required to submit data of bank balances and client level cash and cash equivalents, to the stock exchanges.

14.3. In this regard, the Noticee has submitted that the differences in bank balances were mainly on account of uncleared cheques, which are to be manually excluded from the bank balances. There was inadvertent error in manually computing the balances. With respect to differences in balances of Cash and Cash Equivalents (C&CE), the Noticee has submitted that the differences were due to software issues and various aspects of C&CE which are not required to be reported and not mentioned in the trial balance, such as custody settled accounts, error accounts and bad debt provision accounts. The submissions are provided in detail in sub-paragraph 13.6 above.

14.4. I note that the Noticee has admitted the incorrect reporting to the Exchanges and submitted that they were due to software issues and some other aspects.

14.5. With respect to the other aspects, I note that custody settled accounts are not required to be reported in terms of NSE Circular NSE/INSP/44478 dated May 27, 2020, only where the Noticee only does proprietary trading or all the clients are institutional clients / custody settled. However, the Noticee was also having retail clients. Thus, it was required to report these balances. With respect to error accounts, the Noticee's submissions are acceptable. With respect to client accounts with bad debt provisions, I note that such accounts are not allowed to be excluded as per the reporting provisions. Only when such balances are written off from the books of accounts, they are to be excluded from the calculation of all debit balance clients. However, the Noticee has made provisions for these accounts, i.e. they are not fully written off. Thus, the same should have been included by the Noticee.

14.6. Noticee's has submitted that it has already been penalized by the NSE for incorrect reporting of Financial Ledger (clear) in C&CE. I note that the submissions are not acceptable in light of the observations made in sub-paragraph 13.6 above.

14.7. In view of the aforesaid, I note that there has been incorrect reporting in the data regarding bank balances and C&CE. Therefore, I find that the Noticee has violated the provisions of Clause 3.2 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/ CIR/P/2016/95 dated September 26, 2016.

15. <u>Non adherence to the rules of membership</u>

15.1. It was observed from the Noticee's Financial Statements for the FY 2021-22 that the Noticee was involved in certain transactions with its group companies, during the inspection period. Upon perusal, it was observed that the Noticee had advanced loans to its group companies. The cumulative amount of loans given by the Noticee to three group entities during the year 2021-22 amounted to ₹ 2,363.40 crore. Thus, it was alleged that the Noticee has violated the provisions of Rule 8(3)(f) of the SCR Rules, 1957. The summary of the transactions is provided in the table below.

Name of Group Company	**Nature of Transaction**	**Amount (₹ In Lakhs)**	**Relation**
Phillip Commodities India Private Limited	Loan Given in FY 2021-22	2,180	Group Company
Phillip Finance & Investment Services India Private Limited	Loan Given in FY 21-22	96,610	Group Company
Phillip Services India Private Limited	Loan Given in FY 21-22	1,37,550	Group Company
	TOTAL	2,36,340	

15.2. As per Rule 8(3)(f) of the SCR Rules, 1957, a stock broker shall not engage as principal or employee in any business other than that of securities or commodity derivatives, except as a broker or an agent not involving any personal financial liability.

15.3. In this regard, the Noticee has submitted that the Inter-Corporate Deposits (ICDs) were provided to three of its group / associate companies during the inspection period, out of which two were engaged in the securities markets. These ICDs were made out of the owned funds. The ICDs were majorly provided to meet their working capital requirements, for short durations of 3-5 days as well as intra-day loans. At any point of time, the maximum amount of ICDs has never exceeded ₹ 100 crores. As there were many transactions during the inspection period, it has been observed by the inspection team that loans of ₹ 2363.40 crore were made to these companies, which is a cumulative figure and does not represent the actual position of the ICDs made by the Noticee. All the ICDs have been repaid and reasonable interest on the ICDs has been received by the Noticee. Thus, the transactions were made at arms-length and the Noticee has submitted TDS certificates in support of its contention.

15.4. I note that the Noticee had made ICDs with its associates / group companies. The Noticee has also earned interest, and from Form 16A, I note that Phillip Services India Private Limited and Phillip Finance & Investment Services India Private Limited had deducted TDS under section 194A of the Income Tax Act, 1961, which pertains to interest other than interest on securities, with respect to the payments made to the Noticee. In view of the same, Noticee's submission that it had lent to the associate / group companies to earn interest on its surplus funds, is acceptable.

15.5. SEBI Circular No. SMD/Policy/Cir-6 dated May 07, 1997 also clarifies that that borrowing and lending of funds, by a trading member*, in connection with or incidental to or consequential upon the securities business,* would not be disqualified under Rule 8(1)(f) and 8(3)(f) of Securities Contract (Regulations) Rules, 1957.

15.6. Further, NSE Circular No. NSE/COMP/50957 dated January 07, 2022 clarifies that entering into any arrangement for extending loans or giving deposits / advances to any entity, including group companies such as subsidiaries & associates etc., not in connection with or incidental to or consequential upon the securities/ commodity derivatives business, would be construed as non-compliance of Rule 8(1)(f) and 8(3)(f) of Securities Contract (Regulations) Rules, 1957.

15.7. I note that the Hon'ble SAT, in the matter of Magnum Equity Broking Limited vs. National Stock Exchange of India Limited dated November 29, 2023 (Appeal No 461 of 2022), where it was inter-alia observed that *"10. In our view, investment of surplus funds, generated as a consequence of securities business, with an NBFC registered with RBI cannot lead to an inference that the Appellant is engaged as a principal in business other than that of securities involving personal financial liability. The Respondent Committee given a clear finding that the funds were advanced from the account of the Appellant therefore there is no dispute that the funds were their own moneys…."*

15.8. From the aforementioned regulatory provisions, Noticee's submissions and observations of the Hon'ble SAT, I am of the view that the lending of surplus funds, which are generated as a consequence of the securities business, with the intent to earn interest, cannot be considered non-compliance of Rule 8(3)(f) of Securities Contract (Regulations) Rules, 1957. Further, there is no observation that the surplus funds were not owned funds of the Noticee.

15.9. In view of the foregoing, I find that the alleged violation of the provisions of Rule 8(3)(f) of the SCR Rules, 1957, does not stand established.

16. <u>Improper dealing</u>

16.1. It was observed that Exchange approval for trading with CNB Finwiz Private Limited was revoked on November 10, 2021, but last trade date of Phillip Capital through CNB Finwiz Private Limited was January 12, 2022. Further, total turnover of trade during the period November 10, 2021 to January 12,2022 is Rs. 28.12 crores. Thus, it was alleged that the Noticee has violated the provisions of Clause 3 of SEBI Circular SEBI/ MIRSD//Cir-06/2004 dated

January 13, 2004 by with another stock broker without the prior permission of the Exchange.

16.2. As per Clause 3 of SEBI Circular SEBI/ MIRSD//Cir-06/2004 dated January 13, 2004, a broker shall seek prior permission from the stock exchange for dealing with broker / sub-brokers of the same exchange, either for proprietary trading or for trading on behalf of clients.

16.3. In this regard, the Noticee has submitted that it had traded through the broker CNB Finwiz Private Limited and thereafter with Sushil Financial Services Private Limited for its portfolio management services (PMS) activities. In support of its submissions, the Noticee has also provided confirmation from Sushil Financial Services Private Limited that all the accounts have been opened under PMS category. The Noticee has further submitted that as there were delays in opening of the accounts with Sushil Financial Services Private Limited, the Noticee continued trading through CNB Finwiz Private Limited to service its PMS clients and for no other purpose. The Noticee has also submitted that it was always trading through any one of the brokers at all points of time. The Noticee has not traded through CNB Finwiz Private Limited after January 12, 2022.

16.4. The Noticee has also submitted its email communication with the NSE, where the NSE had clarified that the SEBI Circular SEBI/ MIRSD//Cir-06/2004 dated January 13, 2004 is intended for stock brokers but not for portfolio managers hence, prior approval from the exchange is not required for trading through other members solely for the purpose of PMS transactions.

16.5. From the foregoing paragraphs, I find that the Noticee has traded through CNB Finwiz Private Limited and Sushil Financial Services Private Limited for its PMS clients, and not as a broker. Therefore, as clarified by the NSE, it was not required to obtain prior approval from the Exchanges for trading through the brokers on behalf of its PMS clients. Thus, I find that the alleged violation of provisions of SEBI Circular SEBI/ MIRSD//Cir-06/2004 dated January 13, 2004 does not stand established.

17. Cyber security and cyber resilience

17.1. It was observed from the cyber security report submitted by the Noticee to the NSE and certain information obtained from the Noticee, that off-the-shelf products were not STQC certified. It was further observed that Vulnerability Assessment and Penetration testing (VAPT) was not done during the inspection period (April 01, 2021 to November 30, 2022). Thus, it was alleged that the Noticee has violated the provisions of Clause 36, 41 and 42 of SEBI circular SEBI/HO/MIRSD/CIR/ PB/2018/147 dated December 03, 2018.

17.2. As per Clause 36 of SEBI circular SEBI/HO/MIRSD/CIR/PB/2018/147 dated December 03, 2018 - Cyber Security & Cyber Resilience framework for Stock Brokers / Depository Participants, off the shelf products are required to be STQC certified. As per clause 41 of the aforesaid circular, a stock broker shall regularly conduct vulnerability assessment (VA) to detect security vulnerabilities in their IT environments exposed to the internet. As per clause 42 of the aforesaid circular, a stock broker shall, at least once a year, conduct penetration testing of its IT systems, in order to conduct an in-depth evaluation of the security posture of the system.

17.3. The Noticee has submitted that the software vendors of the Noticee are empanelled with the Exchanges, and none of them obtained the STQC certification. While the Noticee has followed up with the vendor, STQC certification has still not been obtained by the Exchange empanelled vendors. With respect to VAPT, the Noticee has submitted copy of email sent to the MCX which contains VAPT Report 2021-22 summary. The Noticee has also provided screenshots of the VAPT Report, which it has uploaded on the NSE's portal for the FY 2022-23. The Noticee has submitted that no observations were made in the letter of communication of findings dated January 12, 2023, and for this reason the VAPT certificates were not submitted previously.

17.4. I note that the STQC is required to be obtained by the software vendors for the softwares being provided to the Noticee. I also note from the Noticee's submissions that the vendors are empanelled with the Exchanges and that the Noticee has been following up with the vendors for the certification, which they have still not received.

17.5. With respect to the VAPT, I note that the certificates / details of the same were not sought from the Noticee in the communication of findings of inspection, vide letter dated January 12, 2023. The Noticee has now submitted the evidence in the form of copy of email sent to the MCX which contains VAPT Report 2021-22 summary. The Noticee has also provided screenshots of the VAPT Report, which it has uploaded on the NSE's portal for the FY 2022-23. Thus, Noticee's submissions are acceptable.

17.6. Therefore, I find that the allegation of violation of the provisions of Clause 36, 41 and 42 of SEBI circular SEBI/HO/MIRSD/CIR/ PB/2018/147 dated December 03, 2018 does not stand established.

18. To summarize the foregoing findings, I conclude that the Noticee has violated the provisions of Clause 3 and Clause 3.2 of Annexure to SEBI Circular No. SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016.

ISSUE II - Do the violations, if any, attract penalty under Section 15A(b) of the SEBI Act, 1992?

19. I note that the above violations make the Noticee liable for monetary penalty under Section 15A(b) of the SEBI Act, 1992, the text of which is reproduced hereunder:

SEBI Act, 1992

Penalty for failure to furnish information, return, etc.

15A. *If any person, who is required under this Act or any rules or regulations made thereunder,—*

(a) …

(b) to file any return or furnish any information, books or other documents within the time specified therefor in the regulations, fails to file return or furnish the same within the time specified therefor in the regulations or who furnishes or files false, incorrect or incomplete information, return, report, books or other documents, he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees.

20. In context of the above, I refer to the observations of Hon'ble Supreme Court in the matter of Chairman, SEBI vs. Shriram Mutual Fund {[2006] 5 SCC 361} wherein the Hon'ble Court had observed: "*In our considered opinion, penalty is attracted as soon as the contravention of the statutory obligation as contemplated by the Act and the Regulations is established and hence the intention of the parties committing such violation becomes wholly irrelevant A breach of civil obligation which attracts penalty in the nature of fine under the provisions of the Act and the*

Regulations would immediately attract the levy of penalty irrespective of the fact whether contravention must made by the defaulter with guilty intention or not."

ISSUE III - If so, what would be the monetary penalty that can be imposed taking into consideration the factors mentioned in Section 15J of SEBI Act, 1992?

21. While determining the quantum of penalty under Section 15A(b) of the SEBI Act, 1992, it is important to consider the factors stipulated in Section 15J of the SEBI Act, 1992, which read as under:

    SEBI Act, 1992

    15J While adjudging quantum of penalty under section 15-I, the adjudicating officer shall have due regard to the following factors, namely

    (a)the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default;

    (b) the amount of loss caused to an investor or group of investors as a result of the default;

    (c) the repetitive nature of the default.

22. The enhanced supervision of stock brokers was inter-alia introduced Monitoring of Clients' Funds lying with the Stock Broker by the Stock Exchanges, through a sophisticated alerting and reconciliation mechanism, to detect any mis-utilisation of clients fund. For this purpose, the stock brokers were required to submit information periodically to the stock exchanges. Although there is no allegation of misuse of clients' funds, it is observed that there were certain instances of submission of incorrect data to the exchanges. The submission of incorrect data may cause the monitoring mechanism through enhanced supervision, to become ineffective.

23. In the present matter, it is noted that no quantifiable figures are available to assess the disproportionate gain or unfair advantage made as a result of the defaults by Noticee. Further, from the material available on record, it may not be possible to ascertain the exact monetary loss to the investors /clients on account of default by Noticee. Further, as per the available records, it is observed that Noticee has not been penalised earlier for any of the aforesaid violations. Thus, violations are not repetitive in nature. However, I cannot ignore the fact that as a SEBI registered intermediary, Noticee was under statutory obligation to comply with the applicable circulars, rules and regulations. The very purpose of the said regulations is to deter wrong doing and promote ethical conduct in the securities market. Thus, such non-compliance deserves and attracts penalty.

ORDER

24. Having considered all the facts and circumstances of the case, the material available on record, the submissions made by Noticees and also the factors mentioned in Section 15J of the SEBI Act, 1992, and also taking into account judgment of the Hon'ble Supreme Court in SEBI vs. Bhavesh Pabari (2019) 5 SCC 90, I, in exercise of the powers conferred upon me under Section 15-I of the SEBI Act and Rule 5 of the Adjudication Rules, hereby impose following penalty upon the Noticee.

Sr. No.	Name of Noticee	Violation provisions	Penal Provisions	Penalty
1	PHILLIP CAPITAL (INDIA) PRIVATE LIMITED	Clause 3 and Clause 3.2 of Annexure to SEBI Circular No. SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016	Section 15A(b) of SEBI Act, 1992	₹ 2,00,000/- (Rupees Two Lakh Only)

25. The Noticee shall remit / pay the said amount of penalty within 45 days of receipt of this order through online payment facility available on the website of SEBI, i.e. www.sebi.gov.in on the following path, by clicking on the payment link:
ENFORCEMENT → Orders → Orders of AO → PAY NOW.

26. In the event of failure to pay the said amount of penalty within 45 days of the receipt of this Order, SEBI may initiate consequential actions including but not limited to recovery proceedings under Section 28A of the SEBI Act, 1992 for realization of the said amount of penalty along with interest thereon, *inter alia*, by attachment and sale of movable and immovable properties.

27. In terms of Rule 6 of the SEBI Adjudication Rules, 1995 and Rule 6 of SCRA Adjudication Rules, 2005, copy of this order is sent to the Noticee and also to the Securities and Exchange Board of India.

DATE: JUNE 25, 2024
PLACE: MUMBAI

BARNALI MUKHERJEE
ADJUDICATING OFFICER