BEFORE THE ADJUDICATING OFFICER
SECURITIES AND EXCHANGE BOARD OF INDIA
(ADJUDICATION ORDER NO: Order/BRK/PR/2022-23/19919

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

In respect of:

Kaynet Capital Limited

C/o. Mr. Amit Shah,
218, New Raviwar Peth,
Laxmi Niwas Building, 1st Floor,
Near Fulwala Chowk,
Pune – 411002

1. BACKGROUND

1.1 A comprehensive joint inspection was conducted by the Securities and Exchange Board of India (hereinafter referred to as "**SEBI**") along with the Multi Commodity Exchange of India Limited (hereinafter, referred to as "**MCX**") into the business of Kaynet Capital Limited (hereinafter referred to as "**Noticee**"), SEBI Registration No. INB011056737 and PAN AABCK3032E. Inspection was conducted for the period of April 1, 2018 to July 12, 2019 (hereinafter, referred to as "**inspection period**") whereby the inspection had started on July 08, 2019 and concluded on July 12, 2019. The inspection had brought out certain irregularities committed by the Noticee and recommended initiation of Adjudication Proceedings.

2. APPOINTMENT OF ADJUDICATING OFFICER

2.1 Upon submission of Inspection report and proposed actions thereto, the competent authority has agreed with the actions recommended and approved the initiation of Adjudication Proceedings. Subsequently, the undersigned was appointed as Adjudicating Officer on July 23, 2021 under section 19 read with sub-section (1) of section 15-I of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as the "**SEBI Act**") and Rule 3 and 5 of the Securities and Exchange Board of India (Procedure for Holding Inquiry and Imposing Penalties) Rules, 1995 (hereinafter referred to as the "**SEBI Rules**") to inquire into and adjudge under Section 23D of Securities Contracts (Regulation) Act, 1956 [hereinafter referred to as "**SC(R)A**"], Sections 15A(b), 15A(c), 15HB, of SEBI Act and Sections 19A (b) & 19G of Depositories Act, 1996 (hereinafter referred to as "**DP Act**") the alleged violations of the Noticee and if satisfied that the Noticee has become liable to penalty, the undersigned may impose such penalty, as deems fit, in terms of Rule 5 of SEBI Rules.

3. SHOW CAUSE NOTICE

3.1 Pursuant to the above mentioned appointment, as required under Rule 4 (1) of SEBI Rules, a Show Cause Notice (hereinafter referred to as "**SCN**") dated July 15, 2022 was issued to the Noticee informing that during the inspection conducted by SEBI, following alleged violations committed by the Noticee were reported.

i. Section 23D of SC(R)A read with Clause 1 of Annexure of SEBI Circular SMD/SED/CIR/93/23321 dated November 18, 1993 and Clause 3 of Annexure of SEBI Circular SEB/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016; (hereinafter referred to as "**Enhanced Supervision Circular**")

ii. Section 23D of SC(R)A read with SEBI Circular SMD/SED/CIR/93/23321 dated November 18, 1993 and Clause 2.5 of Annexure to Enhanced Supervision Circular;

iii. Clause 8.1 of Annexure of Enhanced Supervision Circular and Clause 12 of Annexure of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009;

iv. Clause 2.3 of SEBI Circular MRD/DoP/SE/Cir-11/2008 dated April 17, 2008;

v. Clause 3.2 & 7 of Annexure of Enhanced Supervision Circular read with SEBI Circular CIR/HO/MIRSD/MIRSD2/CIR/P/2017/64 dated June 22, 2017;

vi. Clause 2 & 6.1.1 (g) of Annexure of Enhanced Supervision Circular read with SEBI Circular CIR/HO/MIRSD/MIRSD2/CIR/P/2017/64 dated June 22, 2017;

vii. Rule 15 of Securities Contracts (Regulation) Rules, 1957 [hereinafter referred to as "**SC(R) Rules**"] and Regulation 17 of Securities and Exchange Board of India (Stock Brokers) Regulations, 1992 (hereinafter referred to as "**Stock Brokers Regulations**");

viii. SEBI Circular SEBI/HO/MIRSD/MIRSD1/CIR/P/2017/1 dated September 21, 2017 read with clause A(1) & A(5) of the Code of Conduct read with Regulation 9(f) of the Stock Brokers Regulations;

ix. CDSL Communique no 2017-318; DP Operating Instruction Chapter 11.9;

x. CDSL Operating Instruction 3.4.4;

xi. CDSL Communique 5139 dated August 01, 2015

xii. SEBI Circular CIR/MIRSD/120/2016 dated November 10, 2016 read with SEBI Circular CIR/MIRSD/66/2016 dated July 21, 2016

xiii. DP Operating Instruction chapter 11.9

Further, the Noticee was also informed that aforesaid alleged violations, if established, make the Noticee liable for monetary penalty under Section 23D of SC(R)A, Sections 15A (b) and 15HB of the SEBI Act.

3.2 In view of the above alleged violations, the Noticee was called upon to show cause under Rule 4 (1) of Adjudication Rules as to why an inquiry should not be held against it in terms of Rule 4 of the Adjudication Rules read with section 15-I of the SEBI Act, 1992 and why penalty should not be imposed in terms of SEBI Adjudication Rules and the provisions of Section 23D of SC(R)A, Sections 15HB and 15A (b) of the SEBI Act.

4. REPLY

4.1 The Noticee vide letter dated July 28, 2022 responded to the SCN as under

"Kaynet Capital is a company incorporated under the Companies Act 1956 having its office at C/o. Amit Shah, 218, New Raviwar Peth, Laxmi Niwas Building, 1st Floor, Near Fulwala Chowk, Pune – 411001 (The Company for short) has for acknowledgment of the above referred Show Cause Notice dated 15/07/2022 purported to be under Rule 4(1) of the Securities and Exchange Board of India (Procedure for Holding Inquiry and Imposing Penalties) Rules, 1995 and in response thereto at the interim the company states without prejudice to its claims and contentions as under:

1. At the outset the company states that in response to the SEBI letter dated 23/06/2020 received from Mr. G. Ram Mohan Rao the General

Manager, MIRSD seeking the comments/ explanations of the Noticee on the alleged observations/ findings as set out in Annexure A therein with respect to the inspection of records of the Noticee as Stock Broker and Depository Participant, allegedly conducted by joint team of SEBI, Exchanges and depository officials during July 2019, in the specified format sent by SEBI and the Noticee repeats and reiterates what is stated in reply thereto by the Noticee's Advocates by way of letter Ref. No. 122/TLA/2020 dated 20/07/2020 recording therein as under :

1.1 *That the company denied that the alleged findings/ observations based on an examination of the company's records on a sample basis by the Inspecting Team and the company's submissions made during the course of inspection and that the findings/ observations pointed out in the inspection report were illustrative in nature and were not all inclusive and stated further that the said letter under reply if acted upon would trigger a parallel proceedings as elucidated therein below and hence the same not maintainable and deserved to be withdrawn forthwith.*

1.2 *The Company stated further without prejudice to its rights and contentions, that Bombay Stock Exchange Ltd. (BSE for short) had already commenced the proceedings against the company by issuing a Show cause Notice dated 17.02.2020 which pertain to the same matters in issue raised by SEBI in the said letter replied to by the company wherein SEBI was proposing to go into. that while the company reserved its right to defend/oppose the proceedings initiated by BSE by reserved its right to participate in the same which had already been initiated by BSE it has caused to suspend the use of trading terminals by the company who was thus debarred from trading in the platform of BSE and thus ipso facto the company ceased to be a participant member of BSE at the material point in time and consequentially the registration of* *the company with SEBI was rendered otiose to that extent and hence he company can be out of regulatory jurisdiction of SEBI.*

1.3 *That therefore no action could lie in furtherance of the alleged inspection stated to have been carried out with respect to the said company in July 2019 or at all inasmuch as the said company was already subject to inquiry proceedings in respect of BSE as initiated in which the said company may take up appropriate defense/oppose as may be advised and hence any further proceedings by SEBI will tantamount to parallel proceedings and lead to multiplicity of proceedings and thus the principles of estoppels would apply as far as civil consequences of the alleged violations are concerned and that the doctrine of Double Jeopardy as enshrined in the constitution of India would operate against any provisions of prosecution as against the Company as such in view whereof the Inspection/observations as stated in SEBI letter under reply are rendered infructuous.*

1.4 *The company sated further that Under the circumstances, no useful purpose will be served in meeting the ends of Justice by proceeding in furtherance of the said inspection carried out by SEBI Jointly with the said Exchange which has since commenced inquiry proceedings against the company for the same cause of actions as alleged and therefore the company did not deem it just, proper and necessary to furnish a reply and or comments as to the observations and findings recorded by SEBI at that stage and therefore called upon SEBI to withdraw the said letter under reply forthwith in the interest of justice recording therein that the present reply was purely on the point of Law and was not an admission of any of the observations or findings that are recorded by SEBI and/ or that may be recorded by SEBI, for want of specific traverse and stated specifically that the said reply on behalf of the* *company shall not be construed as if the company had nothing to sate on merit of the case and the company reserved its right to deal with the same appropriately as and when necessary.*

2. *The company therefore states that consequent upon the company being declared as defaulter by way of letter dated 17/02/2020 the access of the said company to the trading platform of BSE was discontinued and thus the membership of the said company was deemed to have been terminated from Bombay Stock Exchange with effect from 17/02/2020 and therefore effective that date the registration of the said company with SEBI was rendered otiose and the company ceased to be subject to the regulatory jurisdiction of SEBI and therefore the entire proceedings initiated as against the Company are rendered infructuous and not tenable in law.*

3. *While the company without prejudice to its claim and contentions reserves its rights to file further additional point to point reply to the said show cause notice issued by you in due course within three weeks here from and the company, most respectfully doth hereby submit that in view of what is stated hereinabove the matter in issue are beyond the Jurisdiction of SEBI and therefore the above show cause Notice dated 15th July 2022 having been rendered otiose and redundant the same may be withdrawn and proceedings be terminated as such forthwith."*

5. PERSONAL HEARING

5.1 Thereafter, vide Personal Hearing Notice dated July 29, 2022, the Noticee was provided with an opportunity of personal hearing on August 11, 2022 however, the Personal Hearing was postponed to August 22, 2022 which got adjourned to August 29, 2022 on the request of the Noticee. The Personal Hearing was conducted on August 29, 2022 wherein Mr. Sanjay Shah, Group Director appeared and made submissions. Mr. Shah informed that they are planning to file a settlement application in the matters in a month's time and hence pleaded that no adverse order may be passed in the meantime against the entities.

5.2 Vide email dated August 30, 2022 the Noticee informed that

> *"without prejudice we have to inform you that we will avail the opportunity for settlement offered under SEBI Settlement scheme 2022.*
>
> *You are therefore requested not to proceed further in the above matter."*

On the same day the Noticee was informed that Settlement Scheme 2022 is only for cases relating to Illiquid Stock Options. However, the case of the Noticee does not relate to Illiquid Stock Options hence, the Noticee was advised to apply for settlement under Securities and Exchange Board of India (Settlement Proceedings) Regulations, 2018.

However, no intimation with respect to Noticee filing settlement application has been received till date. Further, the Noticee had in its reply dated July 28, 2022 had submitted that additional point to point reply to the said show cause Notice will be filed in due course within three weeks, no additional reply has been received from the Noticee. Therefore, the Noticee has been provided with enough time and opportunity, accordingly, the matter is being proceeded with based on the material available on record including the response of the Noticee to SCN and the submissions made during personal hearing.

6. CONSIDERATION OF ISSUES AND FINDINGS

6.1 I have taken into consideration the facts and circumstances of the case and the material made available on record including responses of the Noticee vide letters dated July 20, 2020 and July 28, 2022. Accordingly, the issues that arise for consideration in the present case are as follows:

(i) Whether SEBI has jurisdiction to adjudicate the instant proceedings in view of the Noticee's Membership being terminated by MCX?

(ii) Whether the Noticee has violated the provisions as mentioned at para 3 above?

(iii) Does the violation, if any, on the part of the Noticee attract monetary penalty under section 15HB of SEBI Act? If so, what would the monetary penalty be that can be imposed upon the Noticee?

I now proceed to deal with the issues brought out above: -

7. Issue (i): Whether SEBI has jurisdiction to adjudicate in the instant matter in view of the Noticee's Membership being terminated by BSE?

7.1 The Noticee had submitted that BSE had already commenced the proceedings against the Noticee by issuing Show Cause Notice dated February 17, 2020 which pertain to the same matters in issue raised by SEBI in the said letter under reply wherein SEBI was proposing to go into the issues which had caused to suspend the use of trading in the platform of BSE and thus ipso facto the Noticee ceased to be a participant member of BSE at that point in time and consequently the registration of the Noticee with SEBI is rendered otiose to that extent and hence the Noticee can be said to be out of the regulatory jurisdiction of SEBI. The proceedings are rendered a nullity as being without jurisdiction.

7.2 The contention of the Noticee does not hold any merit as termination of membership by an exchange does not automatically render the registration granted by SEBI cancelled. As per law a certain procedure is laid down for SEBI to examine the matter before deciding to cancel the registration granted by SEBI. Proceedings conducted by exchanges are distinct from the proceedings conducted by SEBI and so are the consequential actions.

In this connection, attention is drawn to Regulation 27 (i) and (ii) of Stock Brokers Regulations which reads as under

Liability for action under the Securities and Exchange Board of India (Intermediaries) Regulations, 2008 *(hereinafter referred to as "**Intermediaries Regulations**")*

27. A stock broker shall be liable for any action as specified in Chapter V of the Securities and Exchange Board of India (Intermediaries) Regulations, 2008 including suspension or cancellation of his certificate of registration as stock broker if he –

(i) ceases to be a member of a stock exchange; or

(ii) has been declared defaulter by stock exchange and not re-admitted as member within a period of six months; or

7.3 As clearly laid down by the above referred provisions of Stock Brokers Regulations, in case where an entity ceases to be member of a stock exchange, the entity becomes liable for actions as specified under Intermediaries Regulations. Further, cancellation of membership by BSE does not absolve the Noticee from the liability laid down by the provisions of SEBI Act, Rules and Regulations made thereunder for the acts i.e., commissions or omissions of the Noticee during the membership. Accordingly, the contention of the Noticee that by virtue of BSE terminating its membership, the Noticee is out of regulatory purview of SEBI is not acceptable.

Further, the Noticee cannot commit violations of SC(R)A, SEBI Act, Rules, Regulations made thereunder and DP Act and take a plea of not being in the regulatory purview. The Noticee is claiming benefit for the violations committed by itself.

SEBI is the ultimate Regulator for Stock Brokers and a Certificate of Registration is granted by SEBI under Stock Brokers Regulations and therefore until the certificate is cancelled the intermediary is liable for actions by SEBI. Therefore, the submission of the Noticee is not being accepted as it is without any merit.

8. Issue (ii): Whether the Noticee has violated the provisions mentioned at paragraph 3 above?

8.1 Non Settlement of Clients' accounts

8.1.1 Findings of inspection report brought out that 23 out of 40 trading days during the period of October 2018 and March 2019, the value of "G" was negative. Which as per Enhanced Supervision Circular indicates that funds of credit balance clients are utilized for settlement obligations of debit balance clients in the said 23 trading days. The Noticee had misutilised the credit client's fund in the range of the amount of Rs. 1.8 Crores to Rs. 11.7 lakhs for the selected sample days.

8.1.2 Further, the Noticee had done inter-client adjustments by making Journal Vouchers (hereinafter referred to as "**JVs**") and also showed transfer of funds from BSE to NSE from the ledger of one of its client namely Verona Capital to other clients namely Ms. Mansi Vora, Ms. Priti Vora and Ms. Mridula Vora totalling to an amount of Rs.12.4 crores on June 30, 2018. These inter-client adjustments and adjustments between BSE and NSE in the ledgers of the aforesaid clients were made in such a way that all their balances become zero debit as on June 30, 2018. However, the Noticee could not provide details of corresponding funds transfer in the bank statements. Therefore, it was alleged that these ledger entries are just book entries made in order to artificially reduce both the credit balance and debit balances of the aforesaid clients. By making such entries the value of credit balances of clients in the enhanced supervision table get artificially reduced thereby the negative value of “G” was shown as positive value of “G”. Further, “J” value was also found to be negative on 39 out of 40 trading days, it indicates the no credit clients' funds has been utilized towards margin obligations of debit balance clients in the sample period.

8.1.3 Attention is drawn to clause 8.1.2 of Enhanced Supervision Circular, which reads as under

“For the purpose of settlement of funds, the mode of transfer of funds shall be by way of electronic funds transfer viz., through National Electronic Funds Transfer (NEFT), Real Time Gross Settlement (RTGS), etc.”

As brought out above, the Noticee did not transfer funds to clients through bank accounts. The Noticee transferred funds between the accounts of clients through book entries. It appears these entries were made to show the value of ‘G’ as positive. In this connection, it is important to note clause 3.3.1 of Enhanced Supervision Circular the relevant portion of which reads as under

“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 G may 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."

As required by clause 3.3.1 of Enhanced Supervision Circular, the Noticee was duty bound to ensure that the total available funds with the Noticee, clearing corporation/ clearing member should always be equal to or greater than Clients' funds as per ledger balance. Instead the Noticee chose to balance client's funds through book entries presumably to cover up the value of 'G' being negative.

Further, as per Clause 12 (i) of Annexure of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009, *"There shall be no inter-client adjustments for the purpose of settlement of the 'running account'."*

In view of the above and in the absence of any explanation from the Noticee other than mere general denial without any supporting material, the allegation that the Noticee has violated Clause 8.1 of Annexure to SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016 and Clause 12 of Annexure of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009 stands established.

8.2 Monthly/ Quarterly settlement of funds and securities

8.2.1 During the inspection it was observed that the Noticee had not settled the accounts of 36 (thirty-six) clients out of total sample of 800 active clients' and the amount involved was to the tune of Rs. 3,32,203.59/-. The amount was retained by the member in excess of the obligation of the clients. It was further observed that the Noticee had not settled the accounts of Inactive clients as mentioned in Table – 1 wherein only credit balances of more than Rs.100/ - have been considered.

Table - 1

Quarter	Inactive Clients (Nos.)	Amount (Rs.)
Jun 18 -Sep 18	937	2,76,24,747.65
Sep 18 - Dec 18	1097	2,89,75,574.23
Dec 18 - Mar19	850	1,14,47,519.60

The inspection report also records that due to huge number of JVs entries made by the Noticee, it could not be ascertained whether the client-wise balances for active and inactive clients may be more than the above.

8.2.2 Attention is drawn to clause 12 of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009

"Running Account Authorization

12. Unless otherwise specifically agreed to by a Client, the settlement of funds/securities shall be done within 24 hours of the payout. However, a client may specifically authorize the stock broker to maintain a running account subject to the following conditions:

……"

Further clause 8.1.1 of Enhanced Supervision Circular, which reads as under

> *"There must be a gap of maximum 90/30 days (as per the choice of client viz. Quarterly/Monthly) between two running account settlements."*

8.2.3 As mentioned above, it was mandatory for the Noticee to settle the accounts of clients within 24 hours of the payout unless otherwise authorised by the client. Furthermore, the maximum gap between two running account settlements cannot be more than 90/ 30 days. However, as brought out above, the Noticee did not settle the accounts of 36 (thirty-six) clients out of total sample of 800 active clients' and the amount involved was to the tune of Rs.3,32,203.59/-. The Noticee did not settle accounts for 3 quarters.

Considering there is no material contrary to the allegation, the allegation that the Noticee has violated SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009 and Clause 8.1 of Annexure of Enhanced Supervision Circular stands established.

8.3 Pledging of Clients Securities

8.3.1 During the inspection, the Noticee had provided statement of loan against shares of Bank's/ NBFC's wherein it was observed that the Noticee had pledged client securities and raised funds to the tune of Rs. 15.13 crores as on March 13, 2019 towards its own/ debit balance clients as given Table – 2 below:

Table - 2

Bank/ NBFC	Amount Outstanding as on 13.03.2019 (Rs.)
HDFC Bank	6,09,17,470.31
Aditya Birla Capital	2,37,91,496.28
Bajaj Finserv	6,66,51,822.06
Total	**15,13,60,788.65**

As per data available with CDSL (1205600000000851 – Client Account) and NSDL (IN30028010098417- Beneficiary Pledge Client Account) as on October 01, 2019, it was observed that the Noticee had pledged client's securities worth Rs. 1.06 Crores. From the records, a copy of which was provided to the Noticee along with SCN, there were 187 instances wherein the Noticee had pledged client's shares.

8.3.2 Further, the Noticee had failed to provide client-wise security-wise breakup (segregation) of pledged securities. Therefore, it was alleged that the amount raised by pledging clients' securities were mis-utilised.

In this connection, attention is drawn to Section 23D of SC(R)A which reads as under

"Penalty for failure to segregate securities or moneys of client or clients.

23D. *If any person, who is registered under section 12 of the Securities and Exchange Board of India Act, 1992 (15 of 1992) as a stock broker or sub-broker, fails to segregate securities or moneys of the client or clients or uses the securities or moneys of a client or clients for self or for any other client, he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one crore rupees."*

and clause 1(E) of SEBI Circular SMD/SED/CIR/93/23321 dated November 18, 1993 which reads as under

*"**REGULATION OF TRANSACTIONS BETWEEN CLIENTS AND BROKERS***

1. *It shall be compulsory for all Member brokers to keep the money of the clients in a separate account and their own money in a separate account. No payment for transactions in which the Member broker is taking a position as a principal will be allowed to be made from the client's account. The above principles and the circumstances under which transfer from client's account to Member broker's account would be allowed are enumerated below.*

…………..

………….

E] Right to lien, set-off etc., not affected. Nothing in this para 1 shall deprive a Member broker of any recourse or right, whether by way of lien, set-off, counter-claim charge or otherwise against moneys standing to the credit of clients account."

Attention is further drawn to clause 2.5 of Annexure of Enhanced Supervision Circular

2.5. As per existing norms, a stock broker is entitled to have a lien on client's securities to the extent of the client's indebtedness to the stock broker and the stock broker may pledge those securities. This pledge can occur only with the explicit authorization of the *client and the stock broker needs to maintain records of such authorisation. Pledge of such securities is permitted, only if, the same is done through Depository system in compliance with Regulation 58 of the SEBI (Depositories and Participants) Regulations,1996. To strengthen the existing mechanism, the stock brokers shall ensure the following:*

2.5.1. Securities of only those clients can be pledged who have a debit balance in their ledger.

2.5.2. Funds raised against such pledged securities for a client shall not exceed the debit balance in the ledger of that particular client.

2.5.3. Funds raised against such pledged securities shall be credited only to the bank account named as "Name of the Stock Broker - Client Account".

8.3.3 As brought out above, a stock broker is entitled to have a lien on client's securities to the extent of the client's indebtedness to the stock broker and the stock broker may pledge those securities. This pledge can occur only with the explicit authorization of the client and the stock broker needs to maintain records of such authorisation. Pledge of such securities is permitted, only if, the same is done through Depository system in compliance with Regulation 58 of the Securities and Exchange Board of India (Depositories and Participants) Regulations,1996 (hereinafter referred to as "**DP Regulations**").

However, in the instant case it did not appear to be the case wherein the securities pertaining to debit balances clients were pledged by the Noticee. In fact, from the available records it is worth noting that the Noticee did not offer any explanation as to why the securities of clients were pledged. Furthermore, the Noticee has also failed to show that the securities of clients were pledged with the authority from respective clients and as per procedure laid down in Regulation 58 of DP Regulations.

In view of the above, there is no other choice but to hold that going by the available records, the Noticee has violated Section 23D of SC(R)A read with SEBI Circular SMD/SED/CIR/93/23321 dated November 18, 1993 and Clause 2.5 of Annexure of Enhanced Supervision Circular.

8.4 Falsification of records w.r.t. funds

8.4.1 Inspection had brought out instances wherein the Noticee had transferred funds to its group entities which have membership & trading activities in other exchanges i.e., NSE, MCX and National Commodity & Derivatives Exchange Limited (hereinafter referred to as "**NCDEX**"). Based on the data provided by the Noticee, it was observed that there were Journal Voucher (hereinafter referred to as "**JV**") entries for inter exchange adjustments in the same client code. These JV entries had resulted into falsification of actual ledger balances. Details of JV entries made for the years 2017-18, 2018-19 and 2019-20 are tabulated in Table – 3 below

Table – 3

Exchange	F.Y. 2017-18		
	No. of JV's	**Dr. Amt.**	**Cr. Amt.**
BSE	3289	9,80,16,797.86	9,95,72,770.82
NSE	23824	1,20,85,83,404.46	1,20,86,27,564.85
NCDEX	4	10,00,000.00	10,00,000.00
MCX	705	43,93,175.39	28,37,202.43
Total	**27,822**	**1,31,19,93,377.71**	**1,31,20,37,538.10**

Exchange	F.Y. 2018-19		
	No. of JV's	Dr. Amt.	Cr. Amt.
BSE	4090	41,05,28,084.05	41,44,05,401.20
NSE	19892	1,01,24,58,677.46	1,01,24,58,677.46
NCDEX	2	6,046.00	6,046.00
MCX	169	1,79,26,903.47	1,44,46,028.32
Total	**24,153**	**1,44,09,19,710.98**	**1,44,13,16,152.98**

Exchange	F.Y. 2019-20		
	No. of JV's	Dr. Amt.	Cr. Amt.
BSE	1309	5,75,07,450.53	5,73,27,375.20
NSE	2984	14,97,16,403.28	14,97,16,403.28
NCDEX	0	0	0
MCX	9	1,80,525.33	3,60,600.66
Total	**4,302**	**20,74,04,379.14**	**20,74,04,379.14**

8.4.2 Based on above data, it was observed that the inter segment JVs were made by the Noticee in the same client code due to which available running account balances of client's ledgers of the Noticee were incorrect. From the sample data it was observed that the Noticee had made 27,822 such entries during the year 2017-18 thereby debiting an amount to the tune of Rs. 1,31,19,93,377.71/- and crediting Rs. 1,31,20,37,538.10/-. During the year 2018-19 the Noticee had made 24,153 such entries thereby debiting Rs. 1,44,09,19,710.98/- and crediting Rs. 1,44,13,16,152.98 /-. During the year 2019-20 the Noticee had passed 4302 such entries thereby debiting an amount of Rs. 20,74,04,379.14/- and crediting an amount of Rs. 20,74,04,379.14/-. These inter-se transfers among the exchanges had also changed the ledger balances and thereby trial balances and these have resulted in false depiction of enhanced supervision reporting in all the exchanges. These entries have resulted into false depiction of credit balances and debit balances. Hence, enhanced supervision reporting, running account settlement, pledge status by the Noticee has not depicted correct balances and neither can be ascertained thereby indicating further manipulation of records by the Noticee.

8.4.3 The Noticee had made inter client JVs among one group of clients namely Verona Capital, Ms. Mansi Vora, Ms. Priti Vora and Ms. Mridula Vora without corresponding funds transfer in the bank statements in such a way that all their balances become zero in the ledger. These entries were made in such a way that it reduced both credit balance and debit balance. From the copies of the ledgers it was observed that on April 01, 2018, Verona Capital in BSE had a credit balance of Rs.1,40,33,446/- in BSE account. During the inspection it was noted that vide JV0602269 a debit was made from the account of Verona Capital and the account of Ms. Mansi Vora was credited by Rs.1599044.83/-. Similarly, vide JV0602270 the account of Verona Capital was debited and the account of Ms. Mridula Vora was credited by Rs.153307/-. Inspection report alleged that this modus operandi was adopted in order to make this credit balance zero. The Noticee had made two JV entries on June 30, 2018. Firstly, these two debit entries reduced the balance in the account of Verona Capital in BSE to Rs.12280504.17/- (credit balance). This amount was shown transferred to Verona Capital in NSE by making a debit entry and reducing the balance in the ledger of Verona Capital in BSE to zero. Similar modus operandi was used to reduce the balance of Verona Capital in NSE to zero.

8.4.4 It was observed that as on April 01, 2018 Ms. Mansi Vora had a debit balance of. Rs.15,99,044.83/- in BSE. However, vide JV0602269 the account of Mansi Vora was credited by Rs.1599044.83/- thereby reducing the ledger balance to zero as on June 30, 2018. Similarly, in case of Ms. Mridula Vora, as on May 08, 2018 she had debit balance of Rs.1,53,307/- . However, vide JV0602270 her account was credited by Rs. 1,53,307/- thereby reducing the ledger balance to zero as on June 30, 2018. Thus, it was alleged that JV entries were used to reduce both credit balance and debit balances without corresponding fund transfer in bank. These entries will subsequently reduce the credit balances in trial balance and affect enhanced supervision reporting, running account settlement, pledge etc. These details were provided to the Noticee along with SCN.

8.4.5 From the above it is noted that in 3 financial years the Noticee had made 56,277 JVs wherein credit entries were made to the tune of Rs. 2,96,07,58,070.22 and debit entries were made to the tune of Rs. 2,96,03,17,467.83/-. After all this, when given an opportunity to explain these irregularities, the only defense the Noticee had come up with was the baseless argument that the Noticee ceased to be participant member of BSE at the material point in time and consequentially the registration of Noticee with SEBI was rendered otiose to that extent and the Noticee can be said to be out of the regulatory jurisdiction of SEBI.

In view of the above, the Noticee was alleged to have violated SEBI/HO/MIRSD/MIRSD1/CIR/P/2017/104 dated September 21, 2017 and Clauses A(1), A(2), A(4) and A(5) of Stock Broker Regulations.

Clauses A(1), A(2), A(4) and A(5) of Stock Broker Regulations read as follows

"A. General.

(1) Integrity: A stock-broker, shall maintain high standards of integrity, promptitude and fairness in the conduct of all his business.

(2) Exercise of due skill and care: A stock-broker shall act with due skill, care and diligence in the conduct of all his business.

(4) Malpractices: A stock-broker shall not create false market either singly or in concert with others or indulge in any act detrimental to the investors interest or which leads to interference with the fair and

smooth functioning of the market. A stockbroker shall not involve himself in excessive speculative business in the market beyond reasonable levels not commensurate with his financial soundness.

(5) *Compliance with statutory requirements: A stock-broker shall abide by all the provisions of the Act and the rules, regulations issued by the Government, the Board and the Stock Exchange from time to time as may be applicable to him."*

From the above discussion I have no hesitation in holding that the Noticee did not maintain any standard of integrity, did not exercise due skill and care, adopted malpractices to the detriment of its clients in specific and to the securities market in general and continued business in complete disregard to statutory provisions. Consequently, I find the Noticee has violated Clauses A(1), A(2), A(4) and A(5) of Stock Broker Regulations.

8.5 Stock Reconciliation

8.5.1 During the inspection, the verification of the clients' securities from the Statement of Holding of Depository Participant with Statement of Holding of Stock broker as October 01, 2019 following Mis-match was observed: -

i) in about 300 instances, 8,86,835 clients' securities the value of which were to the tune of Rs. 6,48,20,309 were shown in the back office system of the Noticee however, corresponding securities details were not available in DP accounts. Details of these instances were provided to the Noticee along with the SCN. Likewise, as on as on October 01, 2019, in about 240 instances, there were 10,57,974 securities the value of which were to the tune of Rs. 50,13,037.00 were shown in DP accounts however there were no corresponding records in the back office system of the Noticee. Details of the same were provided to the Noticee along with the SCN. Furthermore, the

Noticee made entries however could not provide corresponding bank statements.

ii) the Noticee had not opened Client Unpaid Securities Account (CUSA) and not reported to the Exchange.

iii) the Noticee had not made weekly holding submissions after October 05, 2019 onwards.

In the absence of any explanation from the Noticee on the allegation mentioned above, there is no choice but to hold that the Noticee had violated Clause 2.3 of SEBI Circular MRD/DoP/SE/Cir- 11/2008 which mandates that

> *"2.3 The records should be periodically reconciled with the actual collateral deposited with the broker."*

Further the allegation that the Noticee had violated Clause 2.3 of SEBI Circular dated April 17, 2008 and Enhanced Supervision Circular which was issued to cover *inter-alia* 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 stands established. The Enhanced Supervision Circular in detail lays down the procedures to be followed by Stock Brokers and Depository Participants. The Noticee has flouted and has not followed any of the procedures.

8.6 Enhanced Supervision Reporting

8.6.1 During inspection it was observed that the details of funds and securities of all clients have not been uploaded on Monthly basis under Monitoring of Clients Funds and Securities under Enhanced Supervision. Details of such instances are given in Table – 4 below

Table – 4

S. No.	Month	Count of Client
1	31-Dec-19	2715
2	29-Nov-19	2824
3	31-Oct-19	2933
4	30-Sep-19	3050
5	30-Aug-19	322
6	31-Jul-19	389

8.6.2 It was observed that the Noticee had not made submission of Weekly- Client Assets and Monthly- Monitoring of Client Funds & Securities under Enhanced Supervision reporting from September 2019 and 14 Demat Accounts were not reported under Enhanced Supervision Submission. Details are as given in Table – 5 below

Table – 5

S. No.	NSDL/ CDSL	DP ID	Client Id	Type of Account	Status	Remarks
1	NSDL	IN302164	10404296	Client Beneficiary	SUSPENDED FOR DEBIT	
2	NSDL	IN302164	10389191	Client Beneficiary	SUSPENDED FOR DEBIT	
3	NSDL	IN302662	10153025	Client Beneficiary	CLOSED	
4	NSDL	IN302164	10190015	Client Beneficiary	SUSPENDED FOR DEBIT	
5	NSDL	IN302927	10186677	Client Beneficiary	ACTIVE	
6	CDSL	11000010	00018245	Clearing Member	Active	
7	CDSL	12056000	00002082	CM Pool	Closed	

8	CDSL	12056000	00028016	Regular BO	Closed	
9	CDSL	12056000	00063087	Client Account	Active	Frozen for Both Debit And Credit
10	CDSL	12056000	00164934	Client Account	Active	Frozen for Both Debit And Credit
11	CDSL	12056000	00049661	CM Pool	Closed	
12	CDSL	12056000	00049676	CM Pool	Closed	
13	CDSL	12056000	00049680	CM Principal	Closed	
14	CDSL	12056000	00044551	Regular BO	Closed	

8.7 Maintenance of Books of Accounts & Records

8.7.1 It was also alleged that the Noticee had not maintained proper books of accounts i.e., Client Ledgers, Bank Books, Margin Deposit Books, Sauda Book which is in violation of Rule 15 of SC(R) Rules and Regulation 17 of Stock Brokers Regulations.

The above allegation is general in nature without any specific instances, hence no observations are being made on this allegation.

9. Depository Operations of the Noticee

9.1 W.r.t. Depository Operations of the Noticee, it was observed that the Tariff Sheets Terms and Conditions of the Noticee contained a clause that "Delayed payment charges @ 21% p.a. or such other rate as may be applicable and intimated to the Client from time to time chargeable on the Client's daily debit balance will be borne by the Client" which is in violation of communiqué no. 2017-318, DP Operating Instruction chapter 11.9 wherein it was prescribed that the DPs may levy an interest of not more than 13% p.a. for default in the payment of dues by Beneficiary Owner.

Further, this non-compliance was also observed in the previous year inspection report however, the Noticee continued its non-compliance.

9.2 It was noticed that in case of 44 Beneficiary Owner Identification Numbers out of 53 Beneficiary Owner Identification Numbers it was noticed that Power of Attorneys were in favour of Kaynet Finance Limited which is a group entity of the Noticee. However these were linked to Master POA ID 2205600000000014 which pertains to the Noticee which is in violation of CDSL Operating Instruction 3.4.4.

9.3 It was observed that the Noticee had not incorporated necessary systems and procedures to comply with the SEBI directive with regard to capturing of separate mobile number and email address which is in violation of Communique CDSL/OPS/DP/ POLCY/5139 dated August 01, 2015.

9.4 Concurrent Audit Reports submitted by the auditor of the Noticee were not as per format given in CDSL communiqué no. CDSL/A,I&C/DP/POLCY/ 2018/205 April 18, 2018. The said non-compliance was also observed in the last year inspection report. The Noticee had submitted compliance report stating that the Concurrent Audit Reports were revised as per format. However, it was observed that the Noticee had submitted wrong compliance for the same deviation pointed out during last inspection which is violation of the said Communique of CDSL.

9.5 As far as DP Operations of the Noticee are concerned, the inspection had brought out that while the communiqué no. 2017-318, DP Operating Instruction chapter 11.9 allows DP to levy an interest of not more than 13% p.a. for default in the payment of dues by Beneficiary Owner, the Noticee was charging 21% interest. The Noticee continued to charge 8% higher interest than what was allowed despite being pointed out in previous inspection. Further, the Noticee had not incorporated necessary systems and procedures to comply with the SEBI directive with regard to capturing of separate mobile number and email address in violation of Communique CDSL/OPS/DP/POLCY/5139 dated August 01, 2015. Alarmingly, the

Noticee held POA and Concurrent Audit Reports submitted by the auditor of the Noticee were not as per format given in CDSL communiqué no. CDSL/A,I&C/DP/POLCY/2018/205 April 18, 2018

10. Issue (iii): - Does the violation, if any, on the part of the Noticee attract monetary penalty under section 15HB of SEBI Act? If so, what would the monetary penalty be that can be imposed upon the Noticee?

10.1 In view of the aforesaid discussion at pre paras, it has been established that the Noticee has violated various provision(s) of SC(R)A, SEBI Act, Stock Brokers Regulations, DP Regulations, various clauses of the Circulars as discussed and consequently the Noticee has become liable for imposition of monetary penalty under Section 23D of SC(R) A, Sections 15A (b) and 15 HB of SEBI Act which read as under:

Section 23D of SC(R) A

"Penalty for failure to segregate securities or moneys of client or clients.

23D. If any person, who is registered under section 12 of the Securities and Exchange Board of India Act, 1992 (15 of 1992) as a stock broker or sub-broker, fails to segregate securities or moneys of the client or clients or uses the securities or moneys of a client or clients for self or for any other client, he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one crore rupees."

Sections 15A (b) and 15 HB of SEBI Act

"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, —

.....

(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."

"15HB. Whoever fails to comply with any provision of this Act, the rules or the regulations made or directions issued by the Board thereunder for which no separate penalty has been provided, shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one crore rupees."

10.2 In this regard, reliance is placed upon the order of the Hon'ble Supreme Court of India in the matter of *Chairman, SEBI Vs Shriram Mutual Fund {[2006]5 SCC 361}* – wherein the Hon'ble Supreme Court of India held that

"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…………..."

11. ORDER

11.1 After taking into consideration the facts and circumstances of the case, the discussion in the preceding paragraphs and the factors mentioned in

Section 15 J of SEBI Act, in exercise of the powers conferred upon me under Section 15 I of the Securities and Exchange Board of India Act, I hereby impose a Consolidated penalty of Rs. 25,00,000/- (Rupees Twenty-Five Lakhs only) on Kaynet Capital Private Limited, the Noticee herein for the violations of Section 23D of SC(R)A read with

(i) Regulation 21(1) of Securities and Exchange Board of India (Stock Brokers) Regulations, 1992;

(ii) Clause 2.5 of Annexure of SEBI Circular SMD/SED/CIR/93/23321 dated November 18, 1993;

(iii) Clause 3 of Annexure of SEBI Circular SEB/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016;

(iv) Clause 8.1 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016;

(v) Clause 12 of Annexure of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009;

(vi) Clause III and IV of SEBI Circular CIR/HO/MIRSD/MIRSD2/CIR/P/2017/108 dated September 26, 2017;

(vi) Clause 6.1.1(a) of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016;

(vii) Clause 6.1.1(j) of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016;

(viii) Clause 3 (iii) of SEBI Circular SEBI/HO/CDMRD/DRMP/CIR/P/2016/80 dated September 07, 2016 and Regulation 27(i) and (ii) of Stock Brokers Regulations.

11.2 I am of the considered view that the said penalty is commensurate with the violations, Non Compliances, lapse/ omission on the part of the Noticee.

11.3 The Noticee shall remit / pay the said amount of penalty within 45 (forty five) days of the receipt of this order either by way of Demand Draft (DD) in favour of "SEBI - Penalties Remittable to Government of India", payable at Mumbai and the said DD should be forwarded to the Division Chief, Enforcement Department -I (EFD), Division of Regulatory Action - 3 [EFD1-DRA-3] SEBI Bhavan -II, Plot No. C-7, Block 'G', Bandra Kurla Complex (BKC), Bandra (East), Mumbai – 400 051 and also send an email to tad@sebi.gov.in with the following details:

1	Case Name	
2	Name of the Payee	
3	Date of Payment	
4	Amount Paid	
5	Transaction No.	
6	Bank Details in which payment is made	
7	Payment is made for (penalties/ disgorgement/ recovery/ settlement amount and legal charges along with order details)	

Payment can also be made online by following the below path at SEBI website www.sebi.gov.in ENFORCEMENT → Orders → Orders of AO → Click on PAY NOW or at https://siportal.sebi.gov.in/intermediary/AOPaymentGateway.html

11.4 In the event of failure to pay the said amount of penalty within 45 days of the receipt of this Order, recovery proceedings may be initiated under section 28A of the Securities and Exchange Board of India 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.

11.5 In terms of the provisions of rule 6 of Securities and Exchange Board of India (Procedure for Holding Inquiry and Imposing Penalties) Rules, 1995, a copy of this order is being sent to the Noticee and to the Securities and Exchange Board of India.

BHAVANA RAVIKUMAR

GENERAL MANAGER & ADJUDICATING OFFICER

Place: Mumbai

Date: September 30, 2022