BEFORE THE ADJUDICATING OFFICER
SECURITIES AND EXCHANGE BOARD OF INDIA
(ADJUDICATION ORDER NO: Order/BRK/PR/2022-23/19887

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 Finance Limited

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

1. BACKGROUND

1.1 Securities and Exchange Board of India (hereinafter, referred to as "**SEBI**") along with Bombay Stock Exchange (hereinafter referred to as "**BSE**"), National Stock Exchange of India Limited (hereinafter referred to as "**NSE**"), Multi Commodity Exchange of India (hereinafter referred to as "**MCX**") and Central Depository Services Ltd. (hereinafter referred to as "**CDSL**") conducted a comprehensive joint inspection for the period April 01, 2018 to June 30, 2019 (hereinafter referred to as "**inspection period**") of Kaynet Finance Limited (hereinafter referred to as "**Noticee**"). The Noticee was a Member of NSE and is registered with SEBI as Stock Broker with Registration no. INB/F231276339 and PAN AAACK3482B. The said inspection was conducted from July 08, 2019 to July 12, 2019.

1.2 Pursuant to the completion of inspection, the findings of inspection were communicated to the Noticee vide letter dated June 23, 2020. The Noticee vide letter dated July 20, 2020 responded to the same.

2. APPOINTMENT OF ADJUDICATING OFFICER

2.1 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 "**Adjudication 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) and 15HB, of SEBI Act the following alleged violations of the Noticee and if satisfied that the Noticee has become liable to penalty, the undersigned may impose such penalty, as deemed fit, in terms of Rule 5 of Adjudication 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 said inspection, 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 of SEBI Circular MRD/

DoP/SE/Cir-11/2008 dated April 17, 2008 and clause 2.4 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 2.6 of Enhanced Supervision Circular read with Clause 2(d) of SEBI Circular CIR/HO/MIRSD/MIRSD2/CIR/P/2017/64 dated June 22, 2017;

v. Clause 2 of SEBI Circular MRD/DoP/SE/Cir-11/2008 dated April 17, 2008

vi. 6.1.1 (j) of Annexure of Enhanced Supervision Circular

vii. SEBI Circular CIR/DNPD/7/2011 dated August 10, 2011

viii. 6.1.1 (j) of Annexure of Enhanced Supervision Circular

ix. 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 Securities and Exchange Board of India (Stock Brokers) Regulations, 1992 (hereinafter referred to as "**Stock Brokers Regulations**");

x. Regulation 3 (2) of Securities and Exchange Board of India (Certification of Associated Persons in the Securities Market) Regulations, 2007

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 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 Finance Limited 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, Securities Exchange Board of India seeking the company's comments/ explanations on the alleged observations/ findings as set out in Annexure "A" therein with respect to the inspection of records of the company 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 company repeats and reiterates what is stated in reply thereto by the company's Advocates by way of letter Ref. No. 124/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 was not maintainable and deserved to be withdrawn forthwith.

1.2 *That without prejudice to its rights and contentions, it was stated that NSE wherein the company was a member had already expelled the company from its membership vide letter dated 13/02/2020 therefore though the company was reserving its rights to challenge the same the registration of the company with SEBI was rendered otiose to that extent and hence the company can be out of the regulatory jurisdiction of SEBI.*

The company stated with utmost respect to SEBI that no action can lie in furtherance of the alleged inspection stated to have been carried out with respect to the company in July 2019 or at all inasmuch as the said company was already been awarded the maximum punishment of expulsion from the membership by the NSE 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 and as such the finding and observations as recorded in SEBI letter under reply were rendered infructuous.

1.4 *That Under the circumstances, the company stated with humility that no useful purpose would be served in meeting the ends of Justice by proceeding in furtherance of the said inspection carried* *out by SEBI Jointly with the said Exchanges which has already expelled the said company from its membership for the same cause of action as alleged and therefore the company id not deem it just, proper and necessary to furnish a reply and or comments as to the observations and findings recorded by SEBI at this stage and had thus called upon SEBI to withdraw the said letter under reply. forthwith in the interest of justice.*

1.5 That pertinently it was stated on behalf of the company that the said 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 SEBI for want of specific traverse. The company specifically stated that the said reply on behalf of the company shall be construed as if the company had nothing to state 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 expelled from membership of NSE by way of letter dated 13/02/2020 the access of the said company to the trading platform of NSE was discontinued and thus the aid 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 a member of NSE with effect from 13/02/2020 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 referred show cause Notice dated 15th July 2022 having been rendered otiose and redundant the same may be withdrawn and the 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 matter 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 response of the Noticee vide letter dated July 28, 2020. 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 NSE?

7.1 The Noticee had submitted that NSE had already commenced the proceedings against the Noticee by issuing Show Cause Notice dated February 13, 2020 which pertain to the same matters in issue raised by SEBI wherein SEBI is proposing to go into the issues which had caused to suspend the use of trading in the platform of NSE and thus ipso facto the Noticee ceased to be a participant member of NSE 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 NSE 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 NSE 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 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 accepted as it is without any merit.

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

8.1 Misuse of client funds

8.1.1 Findings of inspection report brought out that 37 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 37 trading days. The Noticee had mis-utilised the credit client's fund in the range of the amount of Rs. 11.5 Crores to Rs. 18.2 crores 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 done 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 that credit clients' funds has been utilized towards margin obligations of debit balance clients in the sample period. Details of these transactions were provided to the Noticee along with the SCN.

8.1.3 In view of the above, it was alleged that the Noticee has violated Section 23D of SC(R)A read with Clause 1 of SEBI Circular SMD/SED/CIR/93/ 23321 dated November 18, 1993 and Clause 3 of Annexure of Enhanced Supervision Circular. The provisions alleged to have been violated 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."*

Clause 1 of SEBI Circular SMD/SED/CIR/93/ 23321 dated November 18, 1993

"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.

A] Member Broker to keep Accounts: Every member broker shall keep such books of accounts, as will be necessary, to show and distinguish in connection with his business as a member -

i. Moneys received from or on account of each of his clients and,

ii. the moneys received and the moneys paid on Member's own account.

B] Obligation to pay money into "clients accounts". Every member broker who holds or receives money on account of a client shall forthwith pay such money to current or deposit account at bank to be kept in the name of the member in the title of which the word "clients" shall appear (hereinafter referred to as "clients account"). Member broker may keep one consolidated clients account for all the clients or accounts in the name of each client, as he thinks fit: Provided that when a Member broker receives a cheque or draft representing in part money belonging to the client and in part money due to the Member, he shall pay the whole of such cheque or draft into the clients account and effect subsequent transfer as laid down below in para D (ii).

C] What moneys to be paid into "clients account". No money shall be paid into clients account other than -

i. money held or received on account of clients;

ii. *such money belonging to the Member as may be necessary for the purpose of opening or maintaining the account;*

iii. *money for replacement of any sum which may by mistake or accident have been drawn from the account in contravention of para D given below;*

iv. *a cheque or draft received by the Member representing in part money belonging to the client and in part money due to the Member.*

D] What moneys to be withdrawn from "clients account". No money shall be drawn from clients account other than -

i. *money properly required for payment to or on behalf of clients or for or towards payment of a debt due to the Member from clients or money drawn on client's authority, or money in respect of which there is a liability of clients to the Member, provided that money so drawn shall not in any case exceed the total of the money so held for the time being for such each client;*

ii. *such money belonging to the Member as may have been paid into the client account under para 1 C [ii] or 1 C [iv] given above;*

iii. *money which may by mistake or accident have been paid into such account in contravention of para C above.*

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.

Clause 3.3.1 of Annexure of Enhanced Supervision Circular

"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."

8.1.4 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 are always 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. As brought out in the Inspection

Report, the Noticee had made inter-client adjustments and adjustments between BSE and NSE to the tune of Rs. 12.4 crores.

8.1.5 As extracted above, as per Section 23 D of SC(R)A, a stock broker shall segregate securities or moneys of clients. However, Clause 1 of SEBI Circular SMD/SED/CIR/93/ 23321 dated November 18, 1993 enumerates the circumstances under which transfer from client's account to Member broker's account would be allowed. 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.

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.

8.1.6 In the absence of any explanation from the Noticee to justify the adjustment made between the accounts, there is no 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 2.4 of Annexure of Enhanced Supervision Circular.

8.2 Monthly/ Quarterly settlement of funds and securities

8.2.1 During the inspection it was found that the Noticee had not settled the accounts of 5 (five) clients out of total sample of 50 active clients the value of the accounts amounting to Rs. 7,26,05,607.58/- the details of which were provided to the Noticee along with the SCN. It was found that the amount was retained by the Noticee in excess of the obligation of these clients. Further w.r.t. the accounts of inactive clients it was found that the Noticee had not settled credit balance of the clients for more than 90 days as summarised in Table – 1 below which remained outstanding for at least two consecutive quarters. The details of which were provided to the Noticee along with the SCN**.**

<u>Table - 1</u>

Quarter	Inactive Clients	Amount (in Rs)
Jun Sep 18	1527	3,16,37,357.65
Sep Dec 18	1756	1,15,39,149.54
Dec 18 Mar 19	1543	96,38,079.70

The inspection report also observed that there were huge number of Journal Vouchers (hereinafter referred to as "**JV**") entries made by the Noticee because of which it could not be ascertained whether the client-wise balances for inactive and active clients are more than the above.

8.2.2 In view of the above, it was alleged that the Noticee violated SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009 and Clause 8.1 of Annexure of Enhanced Supervision Circular which are extracted below

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:

……"

Clause 8.1.1 of Enhanced Supervision Circular

> *"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 which makes the Noticee liable for violation of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009 and Clause 8.1 of Annexure of Enhanced Supervision Circular.

8.3 Client Funding

8.3.1 During the inspection it was found that the Noticee was involved in fund based activity by allowing 10 clients to take exposure beyond T+2+5 days without recovering the debit balance. The Noticee had funded a total amount of Rs. 10,97,05,857.83/-. Details of client funding were provided in Table-2 below. From the sample client ledger provided by the Noticee it was also found that the Noticee had also levied Delayed Payment Charges of Rs. 2,41,95,431.73.

Table – 2

S. No.	Client Code	Date of highest debit	Debit balance	Date of further exposure	Amount of further exposure	Amount Recover	Funding Amount
1	11200	30-May-19	4,58,23,856.27	17-Jun-19	2,86,226.56	16,214	4,60,93,868.83
2	10304	9-May-19	3,23,45,048.60	21-May-19	3,03,329	1,28,41,604	1,98,06,773.60

3	10105	1-Oct-18	2,50,85,030.00	18-Feb-19	25,45,197	1,15,37,950	1,60,92,277.00
4	10113	7-Jun-19	1,09,79,856.00	19-Jun-19	21,13,599	-	1,30,93,455.00
5	10689	9-Jan-19	1,08,52,843.69	23-Jan-19	18,316	45,24,495	63,46,664.69
6	4004	3-Jun-19	32,09,236.00	17-Jun-19	22,45,045	39,700	54,14,581.00
7	1060	23-Oct-18	12,61,830.68	12-Nov-18	2,67,735	4,38,804	10,90,761.68
8	10206	30-May-19	7,83,561.58	13-Jun-19	2,74,664	2,14,737	8,43,488.58
9	85040	14-Jun-19	9,84,899.52	27-Jun-19	21,96	4,66,776	5,40,092.52
10	6777	18-Feb-19	13,93,551.93	28-Feb-19	80,879	10,90,536	3,83,894.93

8.3.2 In view of the above it was alleged that the Noticee has violated Clause 2.6 of Annexure to Enhanced Supervision Circular read with Clause 2 (d) of SEBI circular Ref no. CIR/HO/MIRSD/MIRSD2/CIR/P/2017/64 dated June 22, 2017 which reads as follows

"SEBI has received further representations from the market participants regarding certain provisions of the aforesaid circular. Based on the discussions with different stakeholders, following clarifications are made:

d. Clause 2.6 stands modified as, "Stock brokers shall not grant further exposure to the clients when debit balances arise out of client's failure to pay the required amount and such debit balances continues beyond the fifth trading day, as reckoned from date of pay-in, except, in accordance with the margin trading facility provided vide SEBI circular CIR/MRD/DP/54/ 2017 dated June 13, 2017 or as may be issued from time to time." This clause would be effective from August 1, 2017."

Considering there is no material contrary to the allegation, the allegation that the Noticee has violated the provisions extracted above stands established.

8.4 Stock Reconciliation

8.4.1 It was found that the Noticee had not reconciled the stock. There was a difference in data reported in Weekly holding, monthly holding with back office holding and Demat holding as shown in **Tables – 3** and **4** below thereby indicating that the clients' securities were mis-utilised by the Noticee. Details of differences were provided to the Noticee along with the SCN

Table – 3

Particular	**ISIN**	**Quantity as per DP**	**Qty-back office**	**Difference in Qty.**	**Difference in Value (in Rs.)**
Excess in DP	171	10,82,382.32	5,17,490	5,64,892.32	18,39,93,675.41
Shortfall in DP	47	3,31,182	5,98,783	2,67,601.00	2,52,88,693.65

Table – 4

Particular	ISIN	As per monthly reporting	As per back office	Qty	Value
Excess in Monthly report	227	5,98,925	3,52,390	2,46,535	3,58,19,537.75
Shortfall in Monthly report	114	4,77,488	8,89,479	4,11,991	5,84,33,759.10

In view of the above it was alleged that the Noticee has violated Clause 2.3 of SEBI Circular MRD/DoP/SE/Cir- 11/2008 dated April 17, 2008 read with Enhanced Supervision Circular which reads as follows

"In continuation of earlier circulars and in order to reiterate the need for brokers to maintain proper records of client collateral and to prevent misuse of client collateral, it is advised that: -

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

8.5 Falsification of records w.r.t. funds

8.5.1 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 and Derivatives Exchange Limited (hereinafter referred to as "**NCDEX**"). Based on the data provided by the Noticee, it was observed that there were JV entries for inter exchange adjustments in the same client code. These JV entries had resulted into falsification of actual ledger balances. 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. 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.

8.5.2 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.15,99,044.83/-. Similarly, vide JV0602270 the account of Verona Capital was debited and the account of Ms. Mridula Vora was credited by Rs.1,53,307/-. Inspection report alleged that these 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.1,22,80,504.17/- (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 were used to reduce the balance of Verona Capital in NSE to zero.

8.5.3 It was observed that as on April 01, 2018 Ms. Mansi Vora had a debit balance of. Rs.1599044.83/- in BSE. However, vide JV0602269 the account of Mansi Vora was credited by Rs.15,99,044.83/- 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. Details of ledger of the Noticee showing the above transactions were provided to the Noticee along with the SCN.

8.5.4 In view of the above it was alleged that the Noticee has violated point (b) of SEBI Circular SEBI/HO/MIRSD/MIRSD1/CIR/P/2017/104 dated September 21, 2017

b. Para 3 C) A. iv. of FMC Circular No. FMC/4/2011/G/30 Ref. No.: Div. III/I/89/07 dated December 16, 2011, which restricted seeking authorization through non-mandatory documents for any adjustment of funds among securities (stock) exchange and commodities exchange, will not be applicable, if such adjustment is within the same broking entity.

8.5.5 From the above discussion it is clear 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 conducted business in complete disregard to statutory provisions. Therefore, I have no hesitation in agreeing with the observation of the Inspection team that the member can transfer funds across segments within an entity but not across separate entities. However, the Noticee had contravened the applicable provisions and transferred funds to its separate entities which have separate membership and trading activities on other exchange platforms such as NSE, MCX and NCDEX. Hence, it is very clear that the Noticee had violated SEBI Circular SEBI/HO/MIRSD/MIRSD1/CIR/P/2017/14 dated September 21, 2017 as alleged.

8.6 Net worth verification

8.6.1 As per the inspection report the Net worth of the Noticee based on trial balance provided as on March 31, 2019 was Rs. 16,78,81,888.32. Detailed calculation provided in as per **Table – 5** below. However, the Noticee failed to submit Net worth certificate to Exchanges. It was further alleged that the Net Worth of the TM has fallen below the Exchange minimum requirement of Rs. 1 Crore.

Table - 5

Particulars	**As calculated by official**
Capital	1,12,71,000.00
Free Reserves	1,36,90,097.53
Total	2,49,61,097.53
Less : Not Allowable Assets	
Fixed Assets	82,32,491.73

Pledged Securities	Nil
Member's Card(including Deposits with Stock Exchange)	Nil
Non-allowable Securities (unlisted securities)	Nil
Bed Deliveries	Nil
Doubtful Debts and Advance	
Overdue for more than 3 months	6,93,27,812.75
Advances given to related party	10,89,91,394.86
Prepaid Expenses, Losses	60,95,220.13
Intangible Assets	
30% Marketable Securities	1,96,066.38
Total Non- Allowable Assets	19,28,42,985.85
Networth as on 31st March 2019	16,78,81,888.32

This act of the Noticee is alleged to be in violation of Clause 6.1.1. (j) of Annexure to Enhanced Supervision Circular which reads as follows

"6.1.1. Monitoring criteria for Stock Brokers

a. Failure to furnish Networth certificate to Stock Exchange within 60 days for half year ending September 30th and half year ending March 31st.

b. Failure to furnish Internal Audit report to Stock Exchanges for half year ending September 30th by November 30th and half year ending March 31st by May 31st.

c. Failure to furnish Annual Audited Accounts by September 30th of the relevant year.

d. Failure to co-operate with the Stock Exchange for conducting inspection by not submitting all the information/records sought within 45 days from the due date specified in the letter of intimation.

e. *Failure to submit data for the half yearly Risk Based Supervision within the time specified by Stock Exchange.*

f. *Failure to assign appropriate Bank and Demat nomenclature within the time specified and to report the same to the Stock Exchanges.*

g. *Failure to report new bank and demat accounts opened by the stock broker to exchanges within the time specified for reporting of such accounts.*

h. *Complaints pending for more than 30 days and total value of which is more than 50 per cent of the Networth of the Broker.*

i. *If, at any point of time, Net worth of the Broker is negative or lower than 75 per cent of the requirement.*

j. *In case stock broker shares incomplete/wrong data or fails to submit data on time.*

k. *Failure to submit financial statements as per timeline prescribed under Companies Act, 2013."*

8.6.2 Net worth Certificate is an important document for Members/ Depository Participants to be furnished to Stock Exchange/ Depository and not furnishing of the same within the prescribed time line is a violation of the provisions of the aforesaid circular and the said alleged violation stands established against the Noticee more so when the Noticee has not offered any explanation for such conduct.

8.7 Incorrect reporting of margin

8.7.1 In sample of 29 clients, the total margin requirement was Rs. 34,39,36,347.76, whereas the Noticee had collected Rs. 20,12,76,105.66 as margin resulting in a shortfall of Rs.14,26,60,242.09. Further, although the Noticee had collected Rs. 5,77,734.79 from the clients as short margin collection penalty, the Noticee had not reported any short collection of margin to the exchange. Details were provided to the Noticee along with the SCN.

As has been the case, the Noticee did not offer any explanation with regard to the allegation of short collection of margin nor was any proof submitted to counter the allegation. As such the charge stands established by itself.

8.7.2 However, collection of short margin and not reporting short margin collection penalty by the Noticee is alleged to be in violation of SEBI Circular CIR/DNPD/7/ 2011 dated August 10, 2011. A reading of the circular indicates that a member who short collects margin or does not collect margin becomes liable for a penalty that shall be imposed by stock exchange.

8.8 Enhanced supervision reporting

8.8.1 The inspection brought out that as on June 28, 2019, the Noticee had incorrectly reported the data towards weekly monitoring of client funds w.r.t. details as mentioned in Table – 6 below and found that the Noticee had under reported debit balance clients to the extent of Rs.7.06 crores.

Table - 6

Particulars	**Submitted**	**Exchange Working**	**Difference**
Total End of the day balance in all Client Bank Accounts	10,99,200	9,12,554.78	1,86,645.22
Total Credit Balance of all clients	11,18,85,208	10,49,42,982.63	69,42,225.37
Total debit balance	18,98,22,524	11,91,98,670.40	7,06,23,853.60

Margin utilized for positions of Credit Balance Clients	15,45,82,844	15,53,12,344.67	-7,29,500.67
Free/ unblocked Collateral deposited with clearing corporation/ clearing member(MF)	1,28,76,973	6,25,41,672.61	-4,96,64,699.61

The Noticee is alleged to have violated Clause 6.1.1 (j) of Enhanced Supervision Circular.

"6. Standard Operating Procedures for Stock Brokers/ Depository Participants - Actions to be contemplated by Stock Exchanges/ Depositories for any event based discrepancies

6.1. As per existing norms, Stock Exchanges /Depositories are required to monitor their members/ depository participants. It has been decided that the Stock Exchanges and Depositories shall frame various event based monitoring criteria based on market dynamics and market intelligence. An illustrative list of such monitoring criterias are given below:

6.1.1. Monitoring criteria for Stock Brokers

j. In case stock broker shares incomplete/wrong data or fails to submit data on time."

8.8.2 A Stock Broker is the most crucial intermediary one who deals with the money of investors. A Stock Broker is also an interface between the Regulator and the investor. On the one hand a Stock Broker is duty bound to comply with the statutes in order to maintain the equilibrium of the market. On the other hand, as agent of its clients, it is mandatory for a

Stock Broker to act with due care and diligence. By not abiding with the requisite laws, the Noticee has failed in fulfilling its obligations as per the conditions for registration as Stock Broker. The Noticee has also failed its clients by not putting systems in place and complying with laws. The Noticee has done injustice to its registration as Stock Broker in every aspect and incorrect reporting of the data towards weekly monitoring of client funds is no exception. In the absence of any explanation or evidence to the contrary, it is more than clear that the Noticee has violated Clause 6.1.1 (j) of Enhanced Supervision Circular.

8.9 Office Management

8.9.1 During the inspection it was also found that the Terminal of the Noticee was operated by corporate manager without valid NCFM/ NISM certification which is a violation of Regulation 3 (2) of Securities and Exchange Board of India (Certification of Associated Persons in the Securities Market) Regulations, 2007 which is extracted below

> ***"Obligation to obtain certificate***
>
> *(2) An associated person on being employed or engaged by an intermediary on or after the date specified by the Board shall obtain the certificate within one year from the date of being employed or engaged by the intermediary."*

8.9.2 Allowing a person without requisite certification to operate the Terminal is a serious issue. The Noticee did not seem to have make any systems in place to ensure the running of its business in compliance with applicable provisions of law. When given an opportunity to explain this violation the Noticee did not address the issue at all. The Notice in its defence could have provided a copy of certification from NCFM/ NISM obtained by the corporate manager. In the absence of any explanation or proof, it is difficult not to agree with the allegation the Noticee has violated Regulation 3 (2) of Securities and Exchange Board of India (Certification of Associated Persons in the Securities Market) Regulations, 2007. As such it is held that the Noticee has violated the said provision.

9. Issue (iii): - Does the violation, if any, on the part of the Noticee attract monetary penalty? If so, what would the monetary penalty be that can be imposed upon the Noticee?

9.1 In view of the above discussion at previous paragraphs, it has been more than clearly established that the Noticee has violated various provision(s) of SC(R)A, SEBI Act, Stock Brokers 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 15HB 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."

9.2 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*…………..."

10. ORDER

10.1 From the above discussion and in the absence of any explanation on merits from the Noticee, all allegations stand established.

10.2 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 Finance Limited, the Noticee herein for the violations of Section 23D of SC(R)A read with

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;

ii. Section 23D of SC(R)A read with SEBI Circular SMD/SED/CIR/93/23321 dated November 18, 1993 and Clause 2 of SEBI Circular MRD/DoP/SE/Cir-11/2008 dated April 17, 2008 and clause 2.4 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 2.6 of Enhanced Supervision Circular read with Clause 2(d) of SEBI Circular CIR/HO/MIRSD/MIRSD2/CIR/P/2017/64 dated June 22, 2017;

v. Clause 2 of SEBI Circular MRD/DoP/SE/Cir-11/2008 dated April 17, 2008

vi. 6.1.1 (a) of Annexure of Enhanced Supervision Circular

vii. SEBI Circular CIR/DNPD/7/2011 dated August 10, 2011

viii. 6.1.1 (j) of Annexure of Enhanced Supervision Circular

ix. 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;

x. Regulation 3 (2) of Securities and Exchange Board of India (Certification of Associated Persons in the Securities Market) Regulations, 2007

10.3 I am of the considered view that the said penalty is commensurate with the violation, Non Compliance, lapse/ omission on the part of the Noticee.

10.4 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

10.5 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.

10.6 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