BEFORE THE ADJUDICATING OFFICER
SECURITIES AND EXCHANGE BOARD OF INDIA
ADJUDICATION ORDER NO. Order/PM/PA/2022-23/16489

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

In respect of:

India Infoline Limited
(Now known as IIFL Securities Ltd.)

Registration no: INZ000164132

A. BACKGROUND

1. India Infoline Limited (hereinafter referred to as **"IIFL"/"Company"/ "Noticee")** is *inter alia* registered with Securities and Exchange Board of India (hereinafter referred to as "**SEBI")** as a member of BSE Limited (hereinafter referred to as "**BSE**"), National Stock Exchange of India Ltd. (hereinafter referred to as "**NSE**"), Multi Commodity Exchange of India Limited (hereinafter referred to as "**MCX-SX**") and United Stock Exchange of India. Further, it is also registered as a (i) depository participant of National Depository Services Limited (NSDL) and Central Depository Services (India) Ltd. (CDSL); (ii) research analyst; (iii) investment advisor; (iv) mutual fund; and (v) portfolio management service provider.

2. SEBI had conducted multiple inspections of the books of accounts of IIFL and found that IIFL had allegedly violated the provisions of SEBI circular bearing reference no. SMD/SED/CIR/93/23321 dated November 18, 1993 (hereinafter referred to as the "**SEBI 1993 Circular**") by:

(i) Failing to segregate its own funds from client funds;

(ii) Misusing credit balance of client funds for debit balance client funds; and

(iii) Not appropriately designating client bank accounts.

3. The details of the inspections undertaken are tabulated below:

#	Type and date of inspection	Period of inspection	Place inspected (if any)	Purpose of inspection
1.	Thematic inspection (Dates of inspection: January 30-31, 2014 to February 03, 2014)	April 01, 2011 to December 31, 2013	B Wing, Trade Centre, Kamala Mills Compound, Off Senapati Bapat Marg, Lower Parel, Mumbai – 400013.	Examine whether IIFL has complied with the provisions of the SEBI 1993 Circular and SEBI circular dated April 17, 2008 with respect to segregation of funds and securities of clients. (this inspection is hereinafter referred to as "**Thematic Inspection**").
2.	Comprehensive inspection along with NSE and BSE (Dates of inspection: August 7, 2014, August 12-13, 2014, August 21-22, 2014, August 26, 2014 and September 19, 2014)	April 01, 2013 to June 30, 2014	Corporate office of IIFL: IIFL Centre, Kamala City, Senapati Bapat Marg, Lower Parel, Mumbai – 400013. Branch office of IIFL: C-34, Ground Floor, Shyam Kamal, C Wing, Agrawal Market, Vile Parle (East), Mumbai – 400057. Branch office of IIFL: Kesar Krupa 1st Floor, above Saraswat Bank, Chandravarkar Road, Borivali (W), Mumbai – 400092. Sub broker office: A-1, Akruti Elegance, 90 Feet Road, Mulund (East) Mumbai – 400081.	Examine whether IIFL has maintained books of accounts and other books in the manner required under the SEBI (Stock Brokers) Regulations, 1992 and complied with the provisions of securities law, regulations, rules, circulars, bye-laws and directions issued by SEBI and the stock exchanges. (this inspection is hereinafter referred to as "**Comprehensive Inspection**").
3.	Supplementary Inspection I	April 01, 2011 to June 30, 2014	Data was requisitioned through emails.	Examination of sample top 20 days with highest pay-in obligation of the Company on proprietary account along with client's obligation to the stock exchange.

#	Type and date of inspection	Period of inspection	Place inspected (if any)	Purpose of inspection
				(this inspection is hereinafter referred to as “**Supplementary Inspection I**”).
4.	Supplementary Inspection II	April 01, 2011 to June 30, 2014	Data was requisitioned through emails.	Examination of sample top 105 days with highest pay-in obligations of the Company on proprietary account and clients obligation to the stock exchange. (this inspection is hereinafter referred to as “**Supplementary Inspection II**”).
5.	Supplementary Inspection III	April 01, 2011 to June 30, 2014 (except the days which were inspected during Supplementary Inspection I and II)	Data was requisitioned through emails.	Examination was carried out to calculate the wrongful gains made by IIFL during the entire period of inspection except the days already inspected during Supplementary Inspection I and II. (this inspection is hereinafter referred to as “**Supplementary Inspection III**”).
6.	Inspection (<u>Dates of inspection</u>: March 27, 30 and 31, 2017)	April 01, 2015 to January 31, 2017	Data was requisitioned through emails.	Examination was carried out to verify whether IIFL has complied with the regulations and circulars issued in respect of segregation of funds and securities of clients. (this inspection is hereinafter referred to as “**March 2017 Inspection**”).

4. Inspection findings of Thematic Inspection, Comprehensive Inspection, Supplementary Inspection I, Supplementary Inspection II and Supplementary Inspection III covering the period from April 01, 2011 to June 30, 2014 are part of the first adjudication proceedings initiated against the Company (hereinafter referred to as “**Adjudication Proceedings 1**”) and inspection findings of the March 2017 Inspection covering the period from April 01, 2015 to January 31, 2017 are part of the second adjudication

proceedings initiated against the Company (hereinafter referred to as "**Adjudication Proceedings 2**"). This adjudication order pertains to Adjudication Proceedings 1.

5. With respect to inspection findings of the Thematic Inspection, the Comprehensive Inspection, the Supplementary Inspection I, and the Supplementary Inspection II, enquiry proceedings were also initiated and show cause notice (hereinafter referred to as "**SCN**") dated May 02, 2017 was served on the Company. Thereafter, IIFL successfully filed settlement applications bearing nos. 4034/2019 and 4038/2019 on May 29, 2019 (hereinafter referred to as "**Settlement Applications**") under SEBI (Settlement of Administrative and Civil Proceedings) Regulations, 2014 (hereinafter referred to as "**Settlement Regulations**") for settling all pending adjudication and enquiry proceedings. Accordingly, in terms of the provisions of the Settlement Regulations, Adjudication Proceedings 1 and Adjudication Proceedings 2 were kept in abeyance till the disposal of Settlement Applications. Subsequently, the said Settlement Applications were rejected by the competent authority and the rejection was communicated to the Company *vide* email sent on August 23, 2021.

6. In light of the above, the undersigned resumed Adjudication Proceedings 1.

B. APPOINTMENT OF ADJUDICATING OFFICER

7. SEBI in exercise of the powers under section 19 of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as the **"SEBI Act"**) appointed the undersigned as the adjudicating officer *vide* order dated June 20, 2018 under section 23-I of Securities Contracts (Regulation) Act, 1956 (hereinafter referred to as "**SCRA**") read with rule 3 of the Securities Contracts (Regulation) (Procedure for Holding Inquiry and Imposing Penalties) Rules, 2005 (hereinafter referred to as the **"SCRA Adjudication Rules"**) to inquire into and adjudge against the Company under section 23D of the SCRA for the alleged violations stated in paragraph 2 above.

C. SHOW CAUSE NOTICE, REPLY AND HEARING

8. A SCN dated October 28, 2021 was served on the Noticee under rule 4 of the SCRA Adjudication Rules to show cause as to why an inquiry should not be initiated and penalty should not be imposed under section 23D for the alleged violations. The allegations levelled in the SCN have been summarized below:

8.1 **<u>Violations observed in the Thematic Inspection:</u>**

(i) During this inspection, analysis with respect to maintenance of separate bank and demat accounts for clients and proprietary funds/securities was carried out. In this regard, it was observed that out of the 45 clients bank account examined, 26 client bank accounts were not titled as “client account”.

(ii) Subsequently, in its response, the Company informed SEBI that it had submitted the request to its bankers for changing the title of the aforesaid 26 client accounts to “client account” and provided supporting document with respect to the same. The Company also informed SEBI that out of the 45 client accounts examined most of the client accounts have been designated as client account. However, on perusal of the aforesaid supporting document, it was observed that 3 client bank accounts were still in the process of changing the title to “client bank account”.

(iii) It was also observed during the inspection that BSE had issued a warning to the Company with respect to the aforesaid issue, however despite the BSE warning, it was observed that the Company had failed to change the title of the bank accounts dealing with client transactions.

In view of the above, it was alleged that the Company has violated provisions of the SEBI 1993 Circular by failing to designate bank accounts used for client transactions as client accounts.

8.2 **Violations observed in the Comprehensive Inspection:**

(i) A joint inspection was carried out by SEBI along with NSE and BSE to ascertain if IIFL was in compliance with the provisions of securities law, regulations, rules, circulars, bye-laws and directions issued by SEBI and the stock exchanges.

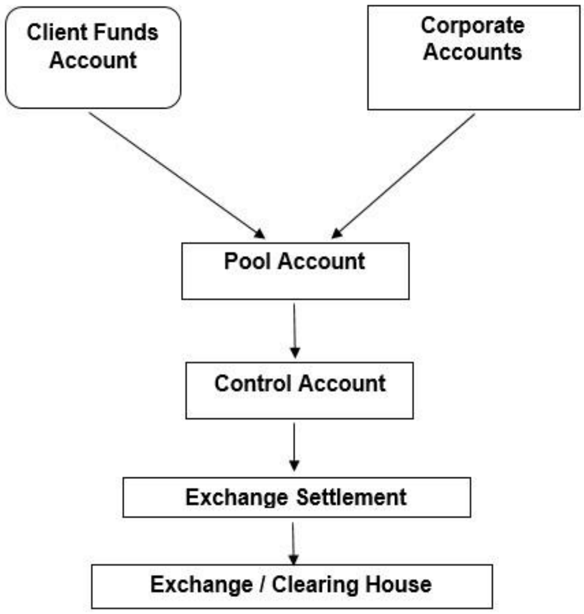
(ii) During the Comprehensive Inspection, IIFL submitted a list of 115 bank accounts which were being used by IIFL for its own, client and settlement purposes as tabulated below:

#	Purpose	No. of accounts
1.	Own*	53
2.	Client	45 including one dividend account bearing no. 004010200982924 maintained with Axis Bank.
3.	Settlement	17
		Total accounts: **115**

**IIFL submitted that the accounts owned by them are categorized in the following manner: salary accounts, business expenses account, administrative account, control accounts, pool account, vendor payment accounts, etc. IIFL also submitted that 24 bank accounts are in the process of closing or have not been used for some time.*

(iii) Further, IIFL informed that it had deposited Rs. 545 crores with NSE, BSE and MCX-SX for doing proprietary trades, however it was also informed by IIFL that it had discontinued proprietary trading in IIFL which was shifted to IIFL Capital Ltd. from the financial year 2014-2015.

(iv) With respect to settlement of funds, during inspection, IIFL submitted that to meet pay-in obligations of clients, funds are transferred from client accounts as well as its own accounts to pool accounts. Subsequently, from the pool accounts, money is transferred to a control account, and from the control account money is eventually transferred to the stock exchange settlement account. The above mechanism is explained through the flowchart given below:



(v) In relation to the above, IIFL also submitted that for NSE capital market segment: *"Funds are pooled into Citi bank account no ending with 9173 (termed as pool account) from all client accounts held with different banks. Funds are also transferred from own bank accounts to said pool accounts so as to ensure fulfillment of pay-in obligations. (This is required to be done as there is generally some time lag in receiving funds from clients e.g. cheques/ instrument in clearing, online transfer of funds not available after NEFT hours etc.)".*

(vi) <u>Observations with respect to the account maintained with Citi Bank bearing no. 340369173</u>

(a) As provided above, during the inspection, it was submitted by the Company that funds were transferred from different client accounts to different pool accounts to control accounts and finally to the settlement account for fulfilling pay-in obligations. In this regard, the Company had also submitted that the key control account was maintained with Citi Bank bearing no. 340369173 (hereinafter referred to as the "**Citi Bank Pool/Control Account**"). Accordingly, the bank book pertaining to the Citi Bank Pool/Control Account was verified by the inspection team for the period April 01, 2013 to June 30, 2014.

(b) The findings of the inspection revealed that funds were regularly being transferred from client bank accounts to the Citi Bank Pool/Control Account which is managed and controlled by IIFL as its own bank account. Further, the inspection team also observed that the Citi Bank Pool/Control Account was *inter alia* being used by IIFL for the following types of transactions:

(b.1) Investments in and redemptions of mutual funds units, investment in bonds, metal trusts and IIFL Income Opportunities Fund.

(b.2) Transfers to and from IIFL Commodities.

(b.3) Transfers to and from for insurance.

(b.4) Transfers to and from IIFL Wealth Management Ltd.

(b.5) Transfers to and from IIFL Realty Ltd.

(b.6) Transfers to and from foreign remittance expenses.

(b.7) Transactions pertaining to fixed deposits, inter-corporate deposits, overdraft, bank charges (for XT-border wire FT) and transactions with other group companies of IIFL, *etc.*

In light of the above paragraph, it was alleged that IIFL has violated provisions of the SEBI 1993 Circular by is mixing its own funds with its client funds in the following manner: (i) by transferring client funds and *its own funds to a common account i.e., Citi Bank Pool/Control Account; and (ii) by using the Citi Bank Pool/Control Account for its own purposes.*

(vii) Observations with respect to the account maintained with Axis Bank bearing no. 4010300022224

(a) During the inspection, along with the Citi Bank Pool/Control Account, an account maintained with Axis Bank bearing no. 4010300022224 (hereinafter referred to as the "**Axis Bank Pool Account**") was examined as the inspecting team was informed by the Company that the aforesaid account is also a pool account. The inspecting team was also informed by the Company that the Axis Bank Pool Account is a pool account because client funds lying in all accounts maintained with Axis Bank are transferred to the Axis Bank Pool Account from which the funds are transferred to the Citi Bank Pool/Control Account. The Company had submitted that the aforesaid transfer of funds to the Axis Bank Pool Account is being undertaken for convenience as a common entry from the Axis Bank Pool Account to the Citi Bank Pool/Control Account could be passed for transferring funds instead of passing entries from multiple accounts maintained with Axis Bank to the Citi Bank Pool/Control Account.

(b) However, during the inspection, it was observed that along with the funds being transferred to the Axis Bank Pool Account from all accounts maintained with Axis Bank and from client dividend account (*i.e.* bank account bearing no. 001010200982924), the Axis Bank Pool Account was *inter alia* being used by IIFL for the following transactions:

(b.1) Transfers to and from client accounts;

(b.2) Transfers from dividend account;

(b.3) Investments in and redemptions of mutual funds units;

(b.4) Transfers to and from bank accounts categorized by IIFL as expenses and salary account;

(b.5) Transactions pertaining to fixed deposit receipts, mutual fund control account, inter-corporate deposits, salary payable, bank guarantee, bank charges and transactions with other group companies of IIFL such as IIFL Capital, IIFL Commodities, IIFL Insurance, *etc.*

(c) Further, it was also observed during inspection that the Company was periodically transferring all receipts from the client dividend account maintained with Axis Bank (*i.e.* bank account bearing no. 001010200982924) to the Axis Bank Pool Account, however, on receipt of dividend on behalf of clients, it should be transferred to the respective personal bank account of the client. In case the client has opted for running account, the dividend may be kept in the client bank account maintained by the Company.

In light of the above, it was alleged that the Company has violated provisions of the SEBI 1993 Circular by mixing its own funds with its client funds by using the Axis Bank Pool Account for its own receipts and payments along with using it for pooling of client funds and dividends.

(viii) <u>Observations with respect to the account maintained with ICICI Bank bearing no. 451000496</u>

(a) It was observed from the inspection that the account maintained with ICICI Bank bearing no. 451000496 ("**ICICI Bank Pool Account**") was being used by the Company for the following segments: BSE cash/futures and options/currency derivatives, NSE currency derivatives/futures and options and MCX-SX currency derivatives/ cash/futures and options.

(b) It was also observed from the Comprehensive Inspection that the ICICI Bank Pool Account was being used by the Company for the following purposes: (i) as a pool account for pooling client funds; (ii) for transferring funds from its own account to ensure fulfilment of pay-in obligations; and (iii) as a control account for transferring funds to other accounts depending upon the requirement of each segment for pay-in obligation from where funds were sent to settlement accounts for meeting pay-in obligation.

(c) However, upon examination of the ICICI Bank Pool Account during inspection, it was observed that the Company apart from using the aforesaid account for the purposes provided above was also using the aforesaid account *inter alia* for carrying out the following transactions:

(c.1) Transfers to and from client accounts;

(c.2) Transactions relating to accounts categorized by IIFL as own-administrative/business operations;

(c.3) Transfers to and from Citi Bank Pool/Control Account and Axis Bank Pool Account and account maintained with HDFC Bank bearing no. 00600130000728;

(c.4) Transaction relating to stock exchange settlement accounts.

Since the ICICI Bank Pool Account was being used as a pool account by the Company where client funds were transferred, it was alleged that IIFL has violated provisions of the SEBI 1993 Circular by mixing its own *funds with its client funds in the following manner: (i) by using the ICICI Bank Pool Account for transacting with the other pool/control accounts owned by the Company such as the Citi Bank Pool/Control Account and Axis Bank Pool Account; and (ii) by using the ICICI Bank Pool Account for its own purposes such as administrative and business operations.*

(ix) <u>Observations with respect to the account maintained with HDFC Bank bearing account no. 00600130000728</u>

(a) During the inspection, the Company had submitted that the account maintained with HDFC Bank bearing account no. 00600130000728 (hereinafter referred to as the "**HDFC Bank Pool Account**") was also used as a pooling account where funds are transferred by the Company from different client accounts.

(b) However, upon examination of the HDFC Bank Pool Account during inspection, it was observed that the Company was using the aforesaid account *inter alia* for carrying out the following transactions:

(b.1) Transfers to and from client accounts;

(b.2) Transactions for vendor payments;

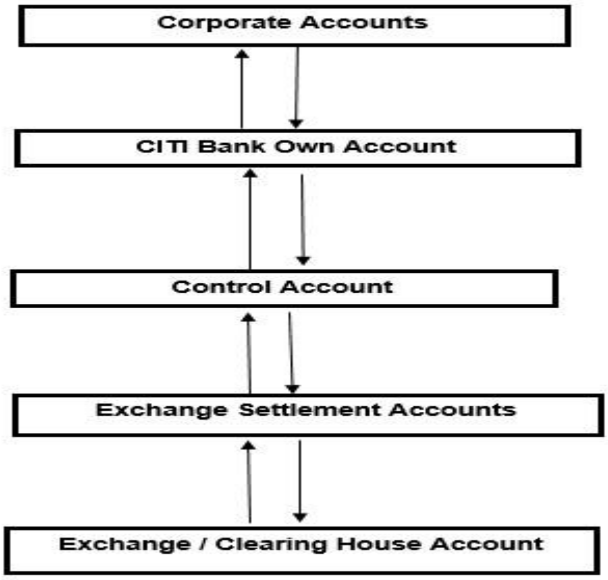
(b.3) Transactions pertaining to salary accounts bearing no. 15770340005705 and 15770340005461; and

(b.4) Mutual fund transactions.

Taking into account the submission made by the Company that the HDFC Bank Pool Bank Account was being used as a pool account by the Company where client funds were transferred, it was alleged that IIFL has violated the provisions of the SEBI 1993 Circular by mixing its own funds with its client funds by using the HDFC Bank Pool Account for its own purposes such as investments, vendor payments, salary etc.

(x) <u>Observations with respect to the proprietary trades carried out by the Company</u>

(a) During the inspection, with respect to proprietary trades, the Company submitted the following flow chart to represent the flow of funds from the Company to the stock exchange/clearing house account:



(b) From the flowchart given above, it was observed during the inspection that funds are transferred from bank accounts owned by the Company to control accounts which is similar to the practice adopted by the Company with respect to the fund movements of its clients (*i.e.,* client funds are firstly transferred to the control account and then to the settlement account of the stock exchange/clearing house).

In light of the above, it was alleged that the Company has violated the provisions of the SEBI 1993 Circular by mixing its own funds with client funds by transferring its own funds and client funds to common pool accounts which are owned by the Company and then to common control accounts which are also owned by the Company.

8.3 Violations observed in Supplementary Inspection I

(i) A supplementary inspection was carried out to ascertain if there was misuse of client funds by the Company. For this purpose, a sample of top 20 days was selected when the Company had the highest pay-in obligation on proprietary account along with client obligation to the stock exchange. Accordingly, the settlement account was examined to ascertain the pay-in obligation of the Company on its proprietary account as well as its client accounts on the selected dates, the details of which are tabulated below:

Financial Year 2012-2013								
Date	Exchange Obligation 2012-13				Prop Obligation 2012-13			
	BSE (Cash & FNO)	NSE (Cash, FNO & CUN)	MCX (CUN)	Total	BSE (Cash & FNO)	NSE (Cash, FNO & CUN)	MCX (CUN)	Total
27/12/2012	-14708655	337437373	-364768	322363950	0	-229482595	183016	-229299579
23/04/2012	-6856462	-297170411	-2871775	-306898648	-6272825	-98686070	1333665	-103625229
26/02/2013	-43497335	-43576724	11905980	-75168079	3529422	-90798364	-5929914	-93198856
21/09/2012	-7684651	663179026	-5608182	649886193	-248456	-91854417	2814506	-89288367
29/08/2012	1249625	9656544	8440357	19346525	-461356	-84542369	-4202405	-89206130
8/5/2012	4703120	-311069082	-1163863	-307529825	-10726189	-76783412	569260	-86940341
8/3/2013	200677429	143733796	-6396817	338014408	-100719915	14324931	3212209	-83182775
11/3/2013	134678818	-67043772	775775	68410821	-67396518	-8834847	-356530	-76587894
23/05/2012	-47985604	119096225	-3687133	67423488	-636198	-73520542	1825839	-72330901
25/03/2013	-3118049	129816397	47507	126745855	-1066658	-70045842	-33081	-71145582

Financial Year 2013-2014								
Date	Exchange obligation 2013-14				Prop obligation 2013-14			
	BSE (Cash & FNO)	NSE (Cash, FNO & CUN)	MCX (CUN)	Total	BSE (Cash & FNO)	NSE (Cash, FNO & CUN)	MCX (CUN)	Total
20/06/2013	-40262643	-330070950	-1479859	-371813452	336800	-122960420	455344	-122168276
18/06/2013	-6980274	101322254	-2574694	91767286	47600	-90167238	1021672	-89097967
9/7/2013	3799474	246775991	76829772	327405238	0	-49010933	-38350135	-87361068
24/06/2013	-36090734	-205238798	17587796	-223741735	146700	-48372819	-8922701	-57148820
23/10/2013	3462201	147129558	0	150591759	0	-55983483	0	-55983483
23/5/2013	-10133722	-146593959	3612084	-153115597	341428	-52927754	-1789836	-54376162
31/05/2013	-18801918	31465816	-1954551	10709347	133556	-53848291	998811	-52715925
11/11/2013	11795089	-68282243	0	-56487154	0	-46499484	0	-46499484
3/6/2013	-50544001	52709595	2175028	4340622	81400	-45443460	-1077266	-46439326
10/6/2013	13572384	-25438205	9499237	-2366584	41200	-39275404	-4782912	-44017116

(ii) During inspection, details were sought from the Company of the payment made through its own accounts for proprietary trades to examine whether client funds were being used by the Company for proprietary trade obligation on the aforesaid sample dates. On perusal of the data submitted by the Company, it was observed that the funds transferred from own account of the Company to the settlement account were less than the proprietary trade obligation of the Company which indicates that the Company did not have sufficient funds to discharge its proprietary trade obligations. It was also observed that in certain instances, funds pay-out from the stock exchange towards client trades were not transferred to the designated “client bank account”.

(iii) *Vide* email dated January 13, 2015 the Company submitted that pay-in and pay-out of funds for client trading and proprietary trading was being routed through the control account for making pay-in/pay-out to/from the settlement account. Further, the Company submitted that funds transferred from its own account to the settlement account was less than its trade obligation as the balance obligation is appropriated out of its own funds lying with the stock exchange. In light of this, the following details were sought from the Company for selected 10 days:

(a) Aggregate value of debit balances of all clients as per trial balance across stock exchange (after adjusting for open bills of clients, uncleared cheques deposited by clients and uncleared cheques issued to clients).

(b) Aggregate value of credit balances of all clients as per trial balance across stock exchange (after adjusting for open bills of clients, uncleared cheques deposited by clients and uncleared cheques issued to clients).

(c) Total fund balance available in all client bank accounts maintained by the Company.

(d) Aggregate value of collateral deposited with clearing corporations in form of cash and cash equivalents (fixed deposits, bank guarantees *etc*.)

(iv) Pursuant to analysis of the aforesaid data submitted by the Company, it was observed that the Company had misused the credit balance of its client funds for pay-out obligations of its debit balance clients. The details of the aforesaid misuse of client funds is provided below:

											In Rs and Crores
#	**Date**	**Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Total of client bank balances**	**Collateral deposited with exchanges by IIFL**				**Total cash available with exchange after adjusted 50% BG**	**Total cash available with broker (E+C=F)**	**Broker used client funds (F-B=G)**
		A	**B**	**C**	**D**			**Total**	**E**	**F**	**G**
1	20/06/2013	247.44	371.06	22.62	70.99	3.5	522	596.49	335.49	358.11	(12.95)
2	21/06/2013	243.13	337.74	30.22	70.99	3.5	522	596.49	335.49	365.71	27.97
3	18/06/2013	199.42	353.83	15.55	51.99	3.5	522	577.49	316.49	332.04	(21.79)
4	19/06/2013	212.84	369.27	13.40	54.99	3.5	522	580.49	319.49	332.89	(36.38)
5	24/06/2013	276.28	326.17	43.03	70.99	3.5	522	596.49	335.49	378.52	52.35
6	25/06/2013	264.49	325.05	25.85	70.99	3.5	522	596.49	335.49	361.34	36.29
7	23/10/2013	167.05	364.23	14.46	1.7	6.85	510	518.55	263.55	278.01	(86.22)
8	24/10/2013	167.52	352.44	8.54	1.7	6.85	510	518.55	263.55	272.09	(80.35)
9	27/12/2012	180.33	423.26	27.73	98.34	2.6	505	605.94	353.44	381.17	(42.09)
10	28/12/2012	182.24	398.18	22.72	20.34	2.6	505	527.94	275.44	298.16	(100.02)

(v) From the table above, it was observed that the total available funds with the Company was less than the ledger credit balance of its clients. (*i.e.*, column F < column B). Further, it was observed that the negative value of column "G" indicates that client funds were utilized by the Company for other purposes *i.e.*, funds of credit balance clients were being utilized for settlement obligations of debit balance clients. It was also observed that out of the selected 10 days, the credit clients funds were misutilized by the Company for settlement obligation of debit balance clients for 7 days.

(vi) From the documents submitted by the Company, it was also observed that pay-in and pay-out of the Company to the stock exchange was taking place through the control accounts. As explained in paragraph 8.2 above, it was observed during the Comprehensive Inspection that control accounts are Company accounts wherein the Company transfers its own funds as well as its client funds leading to mixing of own funds and client funds.

Taking the aforesaid into consideration, it was alleged that the Company has contravened the provisions of the SEBI 1993 Circular by (i) utilizing funds of credit balance clients for settlement obligation of debit balance clients for 7 days from the sample selected; and (ii) mixing client funds with proprietary funds by routing transactions through control accounts.

8.4 **Violations observed in Supplementary Inspection II**

(i) In addition to the samples verified in the previous inspections/ supplementary inspections, in this particular inspection, additional 105 days were selected as samples for examination. The criteria for selecting the aforesaid sample dates was that such dates need to be examined wherein the Company had the highest pay-in obligation to the stock exchanges pursuant to its own account as well as its client accounts as there is more probability of misuse of client funds on days when the Company had maximum obligation. Accordingly, settlement account was verified during this inspection to ascertain the pay-in obligations made by the Company through proprietary bank accounts and client bank accounts for the selected days. The data sought for the aforesaid examination was similar to the data requisitioned in paragraph 8.3(iii) above. On perusal of the data submitted by the Company, it was observed that the Company had misutilized the credit client fund balances for pay-out of settlement obligation of its debit balance clients as well as for proprietary trade obligations, which is tabulated hereunder:

										(In Rs and Crores)
#	**Date**	**Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Total of client bank balances**	**Collateral deposited with exchanges by IIFL**				**Total funds available with broker after adjusted 50% of BG [Client bank balances (C) + Collateral with exchanges i.e cash+ FD +50% BG]**	**Broker used credit client funds for debit clients purpose (E-B=F)**
		A	**B**	**C**	**D**			**Total**	**E**	**F**
					Cash	**FD**	**BG**			
1	10-Mar-14	183.49	337.63	10.94	12.54	7.65	446.10	466.29	254.19	(83.45)
2	13-Mar-12	485.20	646.71	20.25	23.59	28.30	355.10	406.99	249.69	(397.02)
3	6-Jan-12	185.45	407.96	8.30	35.09	22.50	345.10	402.69	238.43	(169.53)
4	16-May-14	266.77	462.27	18.83	75.29	1.65	509.10	586.04	350.32	(111.95)
5	28-Apr-11	352.63	461.97	29.29	35.47	-	270.00	305.47	199.76	(262.20)
6	27-May-14	254.47	541.59	23.73	30.29	1.65	529.10	561.04	320.22	(221.37)
7	13-Jan-12	200.83	423.78	8.01	7.09	32.50	345.10	384.69	220.15	(203.63)
8	8-Aug-11	304.15	476.23	12.71	3.17	-	350.00	353.17	190.88	(285.35)
9	26-Dec-11	196.61	405.04	6.60	7.09	22.50	355.10	384.69	213.74	(191.30)
10	26-Apr-11	388.46	474.46	40.61	15.47	-	270.00	285.47	191.08	(283.38)
11	31-Jan-12	181.77	483.80	6.62	17.09	32.50	345.10	394.69	228.75	(255.05)
12	16-Jun-14	253.45	494.51	28.56	13.29	1.65	538.10	553.04	312.55	(181.96)
13	18-Apr-11	384.33	486.46	25.56	36.12	0.87	253.50	290.49	189.30	(297.16)
14	23-Sep-11	322.89	513.74	19.13	55.59	-	413.60	469.19	281.52	(232.22)
15	10-Jun-14	245.96	569.45	21.55	58.29	1.65	538.10	598.04	350.54	(218.91)
16	23-Feb-12	253.28	527.59	10.60	50.59	28.30	355.10	433.99	267.04	(260.55)
17	11-Apr-14	145.69	375.08	40.68	20.39	1.65	489.10	511.14	307.27	(67.81)
18	5-Jul-12	141.09	404.60	5.92	66.18	0.80	370.10	437.08	257.95	(146.64)

(In Rs and Crores)										
#	Date	Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Total of client bank balances	Collateral deposited with exchanges by IIFL				Total funds available with broker after adjusted 50% of BG [Client bank balances (C) + Collateral with exchanges i.e cash+ FD +50% BG]	Broker used credit client funds for debit clients purpose (E-B=F)
		A	B	C	D			Total	E	F
					Cash	FD	BG			
19	19-May-11	365.95	441.46	26.91	10.47	-	330.00	340.47	202.38	(239.08)
20	13-May-14	93.10	386.13	19.28	40.29	1.65	489.10	531.04	305.77	(80.36)
21	11-Nov-11	302.75	450.19	7.97	7.09	27.50	365.10	399.69	225.10	(225.08)
22	4-Oct-11	277.02	438.65	11.27	5.59	-	413.60	419.19	223.66	(215.00)
23	4-May-11	406.19	436.22	39.06	2.47	-	320.00	322.47	201.53	(234.69)
24	20-Mar-14	156.86	318.16	18.11	20.54	7.65	466.10	494.29	279.35	(38.81)
25	18-Apr-13	169.91	362.95	18.69	42.99	3.50	532.10	578.59	331.23	(31.72)
26	12-Mar-13	216.14	327.01	20.31	17.49	2.50	532.10	552.09	306.35	(20.66)
27	21-Feb-12	236.34	512.16	13.02	48.94	28.30	355.10	432.34	267.81	(244.36)
28	10-Apr-12	181.32	412.17	7.23	23.59	28.30	345.10	396.99	231.67	(180.50)
29	26-Mar-12	509.87	362.99	21.84	39.59	28.30	355.10	422.99	267.28	(95.71)
30	2-May-11	412.13	476.22	29.00	45.47	-	270.00	315.47	209.47	(266.76)
31	5-Sep-11	222.81	418.50	10.43	5.19	10.00	333.60	348.79	192.42	(226.08)
32	29-Aug-11	254.42	381.64	10.96	5.09	-	323.60	328.69	177.84	(203.80)
33	9-Aug-11	303.65	377.66	28.77	25.32	-	383.60	408.92	245.89	(131.78)
34	19-Apr-11	386.31	476.84	20.96	46.12	0.87	253.50	300.49	194.70	(282.14)
35	27-Jul-11	289.79	425.12	9.53	15.61	-	351.70	367.31	200.99	(224.13)
36	16-Jan-12	209.51	414.33	8.35	7.09	32.50	345.10	384.69	220.49	(193.84)
37	13-Sep-11	280.15	452.47	13.02	29.19	10.00	333.60	372.79	219.00	(233.46)
38	27-Mar-12	468.37	347.06	17.04	26.59	28.30	355.10	409.99	249.48	(97.58)
39	12-Sep-11	267.22	449.42	11.69	18.19	10.00	333.60	361.79	206.68	(242.75)

(In Rs and Crores)

#	Date	Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Total of client bank balances	Collateral deposited with exchanges by IIFL				Total funds available with broker after adjusted 50% of BG [Client bank balances (C) + Collateral with exchanges i.e cash+ FD +50% BG]	Broker used credit client funds for debit clients purpose (E-B=F)
		A	B	C	D			Total	E	F
					Cash	FD	BG			
40	2-Nov-11	255.15	493.63	6.49	7.09	20.00	365.10	392.19	216.12	(277.51)
41	20-May-14	298.10	551.26	20.91	100.29	1.65	509.10	611.04	377.41	(173.85)
42	21-Jan-13	232.34	390.21	7.77	13.79	2.60	520.10	536.49	284.22	(105.99)
43	7-Oct-11	233.27	418.90	16.58	5.59	-	413.60	419.19	228.97	(189.94)
44	19-Jun-14	287.13	491.25	21.84	13.29	1.65	538.10	553.04	305.83	(185.42)
45	12-Jun-14	313.95	504.53	32.68	58.29	1.65	538.10	598.04	361.68	(142.85)
46	13-Dec-11	243.59	422.82	8.63	7.09	32.50	355.10	394.69	225.77	(197.05)
47	4-Jul-12	138.36	406.67	6.02	46.07	0.80	345.10	391.97	225.44	(181.24)
48	21-Nov-11	336.92	417.03	26.98	7.09	32.50	365.10	404.69	249.12	(167.91)
49	11-Apr-11	338.46	535.15	12.62	36.12	0.87	253.50	290.49	176.35	(358.80)
50	12-Jul-12	163.42	400.34	8.76	97.87	0.10	400.10	498.07	306.78	(93.56)
51	30-Nov-11	176.04	423.40	7.93	7.09	32.50	345.10	384.69	220.07	(203.33)
52	24-Nov-11	283.99	455.48	16.35	7.09	32.50	345.10	384.69	228.49	(226.99)
53	24-Apr-12	235.74	373.01	7.29	36.08	28.30	325.10	389.48	234.22	(138.79)
54	19-Oct-11	285.16	422.71	9.09	6.59	-	413.60	420.19	222.48	(200.23)
55	27-Sep-11	232.20	485.18	12.39	5.59	-	413.60	419.19	224.77	(260.41)
56	16-Mar-12	517.56	468.58	22.30	20.59	28.30	355.10	403.99	248.74	(219.84)
57	23-May-13	217.25	441.21	13.69	34.99	3.50	532.10	570.59	318.24	(122.98)
58	13-Feb-12	205.07	512.29	13.14	29.09	28.30	345.10	402.49	243.07	(269.22)
59	12-Jun-13	207.41	356.70	11.63	19.99	3.50	522.10	545.59	296.17	(60.53)
60	9-May-12	272.21	346.56	12.05	68.58	13.30	340.10	421.98	263.98	(82.58)
61	4-Apr-13	150.03	323.47	14.96	27.49	2.50	532.10	562.09	311.01	(12.47)

(In Rs and Crores)											
#	**Date**	**Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Total of client bank balances**	**Collateral deposited with exchanges by IIFL**				**Total funds available with broker after adjusted 50% of BG [Client bank balances (C) + Collateral with exchanges i.e cash+ FD +50% BG]**	**Broker used credit client funds for debit clients purpose (E-B=F)**
		A	**B**	**C**	**D**			**Total**	**E**	**F**
					Cash	**FD**	**BG**			
62	25-Jul-13	187.93	349.11	16.41	54.99	3.50	522.10	580.59	335.95	(13.16)
63	1-Mar-13	266.12	326.42	16.33	40.49	2.50	520.10	563.09	319.38	(7.04)
64	9-Dec-11	238.86	446.77	9.28	7.09	32.50	355.10	394.69	226.42	(220.35)
65	12-Mar-14	171.85	353.15	24.61	12.54	7.65	446.10	466.29	267.86	(85.30)
66	4-Dec-12	205.39	470.52	13.90	70.84	2.60	495.10	568.54	334.89	(135.63)
67	30-May-14	293.39	521.20	19.25	14.29	1.65	538.10	554.04	304.24	(216.95)
68	21-Oct-11	297.82	460.52	13.76	6.59	-	413.60	420.19	227.15	(233.38)
69	29-Sep-11	231.97	454.62	10.54	5.59	-	413.60	419.19	222.93	(231.69)
70	27-Sep-12	161.20	471.44	5.69	46.78	2.60	485.10	534.48	297.62	(173.82)
71	14-Sep-11	289.90	450.22	13.28	42.19	10.00	333.60	385.79	232.26	(217.95)
72	19-Aug-13	207.76	324.30	26.03	19.57	0.50	540.10	560.17	316.15	(8.15)
73	21-Jul-11	270.93	424.96	7.48	27.17	-	330.00	357.17	199.65	(225.31)
74	27-Jul-12	187.97	331.00	7.27	5.28	0.10	490.10	495.48	257.70	(73.29)
75	18-Dec-13	175.88	343.67	14.12	6.39	6.85	400.10	413.34	227.41	(116.26)
76	15-Dec-11	247.91	402.96	9.62	7.09	32.50	355.10	394.69	226.75	(176.21)
77	1-Dec-11	181.09	391.66	8.85	7.09	32.50	355.10	394.69	225.99	(165.67)
78	15-Jun-12	155.40	367.97	8.32	34.33	0.80	370.10	405.23	228.50	(139.47)
79	9-Jan-12	274.23	415.18	5.90	7.09	22.50	365.10	394.69	218.03	(197.15)
80	4-Feb-14	207.98	326.60	18.17	2.39	6.85	421.10	430.34	237.96	(88.63)
81	4-Sep-13	195.80	323.34	11.55	14.56	0.50	528.60	543.66	290.91	(32.43)
82	6-May-13	143.39	406.30	5.32	34.99	3.50	532.10	570.59	309.86	(96.44)
83	28-Feb-12	286.09	480.54	9.80	42.09	28.30	355.10	425.49	257.74	(222.80)

(In Rs and Crores)										
#	**Date**	**Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Total of client bank balances**	**Collateral deposited with exchanges by IIFL**				**Total funds available with broker after adjusted 50% of BG** **[Client bank balances (C) + Collateral with exchanges i.e cash+ FD +50% BG]**	**Broker used credit client funds for debit clients purpose** **(E-B=F)**
		A	**B**	**C**	**D**			**Total**	**E**	**F**
					Cash	**FD**	**BG**			
84	23-May-14	306.06	528.30	21.95	40.29	1.65	519.10	561.04	323.44	(204.85)
85	28-May-12	218.70	373.32	8.66	29.58	0.80	370.10	400.48	224.09	(149.23)
86	19-Dec-11	266.97	400.49	10.25	7.09	32.50	355.10	394.69	227.39	(173.10)
87	16-Aug-11	299.36	408.19	10.53	23.83	-	484.40	508.23	276.56	(131.62)
88	3-Jan-14	170.56	389.73	19.76	22.39	6.85	400.10	429.34	249.06	(140.67)
89	24-Jul-12	172.90	372.81	8.29	63.02	0.10	490.10	553.22	316.47	(56.34)
90	25-Oct-12	213.01	428.96	10.62	22.28	2.60	445.10	469.98	258.05	(170.91)
91	27-Aug-12	208.64	384.81	3.87	20.10	2.60	520.10	542.80	286.62	(98.18)
92	28-Aug-13	212.58	296.24	15.04	9.56	0.50	540.10	550.16	295.15	(1.09)
93	4-May-12	237.08	357.37	24.86	49.58	18.30	325.10	392.98	255.29	(102.08)
94	5-Oct-11	262.14	432.60	5.77	5.59	-	413.60	419.19	218.15	(214.45)
95	19-May-14	246.49	417.49	21.70	90.29	1.65	509.10	601.04	368.19	(49.30)
96	17-Jan-13	236.63	410.88	14.24	22.79	2.60	520.10	545.49	299.68	(111.20)
97	20-Mar-12	501.16	427.46	11.27	18.59	28.30	355.10	401.99	235.71	(191.76)
98	28-Sep-12	175.05	444.90	9.79	44.28	2.60	485.10	531.98	299.23	(145.67)
99	17-May-12	249.90	351.19	13.59	53.58	0.80	350.10	404.48	243.03	(108.17)
100	5-Jul-11	260.80	437.31	16.92	11.47	-	330.00	341.47	193.39	(243.92)
101	6-Jun-14	285.67	523.31	18.32	38.29	1.65	538.10	578.04	327.31	(195.99)

(ii) Further, from the analysis of the misuse of funds by the Company it was observed that the total available funds with the Company as provided in column "E" was less than the ledger credit balance of clients as provided in column “B”. The negative value of "F" column (*i.e.,* the difference between the E column and the B column) indicates that the Company had utilized client funds for other purposes *i.e.,* funds of credit balance clients were being utilized for settlement obligations of debit balance clients by the Company. Further, it was observed that out of the sample 105 days, the Company had misutilized the credit client funds for the settlement obligation of debit balance clients for 101 days which amounts to 96% of the total selected sample days. The misutilization of credit client funds by the Company ranged from Rs 1.09 crores to Rs 397.02 crores for the selected sample days.

(iii) It was also observed that out of the 101 days when the Company had misutilized the credit client funds for the settlement obligation of debit balance clients, for 13 days the Company had also used the client funds for settlement obligation of proprietary trades. The details of the same are provided below:

Date	**Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)**	**Total of client bank balances**	**Collateral deposited with exchanges by IIFL**				**Total funds available with broker after adjusted 50% of BG [Client bank balances (C) + collateral with exchanges i.e Cash+FD+50 %BG]**	**Broker used credit client fund for debit clients purpose (E-B=F)**	**Broker used client fund for own purpose (F-A=G)**
	A	**B**	**C**	**D**			**Total**	**E**	**F**	**G**
				Cash	**FD**	**BG**				
13-Jan-12	200.83	423.78	8.01	7.09	32.50	345.10	384.69	220.15	(203.63)	(2.80)
31-Jan-12	181.77	483.80	6.62	17.09	32.50	345.10	394.69	228.75	(255.05)	(73.28)
23-Feb-12	253.28	527.59	10.60	50.59	28.30	355.10	433.99	267.04	(260.55)	(7.27)
5-Jul-12	141.09	404.60	5.92	66.18	0.80	370.10	437.08	257.95	(146.64)	(5.56)
21-Feb-12	236.34	512.16	13.02	48.94	28.30	355.10	432.34	267.81	(244.36)	(8.02)
5-Sep-11	222.81	418.50	10.43	5.19	10.00	333.60	348.79	192.42	(226.08)	(3.27)
2-Nov-11	255.15	493.63	6.49	7.09	20.00	365.10	392.19	216.12	(277.51)	(22.36)
4-Jul-12	138.36	406.67	6.02	46.07	0.80	345.10	391.97	225.44	(181.24)	(42.88)

Date	Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Total of client bank balances	Collateral deposited with exchanges by IIFL				Total funds available with broker after adjusted 50% of BG [Client bank balances (C) + collateral with exchanges i.e Cash+FD+50 %BG]	Broker used credit client fund for debit clients purpose (E-B=F)	Broker used client fund for own purpose (F-A=G)
	A	B	C	D			Total	E	F	G
				Cash	FD	BG				
11-Apr-11	338.46	535.15	12.62	36.12	0.87	253.50	290.49	176.35	(358.80)	(20.33)
30-Nov-11	176.04	423.40	7.93	7.09	32.50	345.10	384.69	220.07	(203.33)	(27.29)
27-Sep-11	232.20	485.18	12.39	5.59	-	413.60	419.19	224.77	(260.41)	(28.21)
13-Feb-12	205.07	512.29	13.14	29.09	28.30	345.10	402.49	243.07	(269.22)	(64.15)
27-Sep-12	161.20	471.44	5.69	46.78	2.60	485.10	534.48	297.62	(173.82)	(12.62)

(iv) From the table provided above, it was observed that the ledger debit balance of the clients (values in column A) was less than the credit clients fund used for the settlement of debit client obligation (values in column F) which suggests that the funds from credit balance client accounts were not entirely used for debit client obligations. Herein, the negative value of "G" column indicates that client funds were utilized by the Company for settlement obligations of proprietary trades and the amount of such misutilization ranged from Rs. 2.02 crores to Rs.73.28 crores.

In summary, it was alleged that the Company has violated the provisions of the SEBI 1993 Circular by: (i) utilizing funds of credit balance clients for settlement obligation of debit balance clients for total 101 days from the sample selected resulting into misutilization of client funds ranging from Rs 1.09 crores to Rs 397.02 crores; (ii) utilizing funds of credit balance clients for settlement obligation of proprietary trades for 13 days from the sample selected resulting into misutilization of client funds ranging from Rs. 2.02 crores to Rs.73.28 crores; and (iii) mixing client funds with proprietary funds by routing transactions through common control accounts.

8.5 **Violations observed in Supplementary Inspection III**

(i) This inspection was undertaken to calculate the wrongful gains made by the Company during the entire inspection period from April 01, 2011 to June 30, 2014 (*i.e.,* 695 trading days) except the days already examined in Supplementary Inspection I and Supplementary Inspection II. For the aforesaid purpose, details were sought from the Company.

(ii) On perusal of the details provided by the Company, it was observed that the Company had misutilsed the credit balance of its client funds for fulfilling settlement obligation of its debit balance clients and for its own purposes. The detailed analysis of the aforesaid 695 days was provided as annexure 15 and 16 with the SCN to the Company. It was observed from annexure 16 that that total funds available with the Company (*i.e.,* column E) was less than the ledger credit balance of the clients (*i.e.,* column B). In the aforesaid annexure, the negative value of "F" column which was arrived at after calculating the difference between the E column and the B column indicated that the Company had utilized client funds for other purposes and therefore the same was not being reflected in the total funds available with the Company *i.e.,* funds of credit balance clients were being utilized for settlement obligations of debit balance clients and proprietary purposes by the Company.

(iii) It was also observed that out of the sample 695 days examined, the Company had misused the credit client funds for the settlement obligation of debit balance clients for 687 days which is 98.85% of the total aforesaid inspection period and the amount of misutilisation ranged from Rs. 0.58 crores to Rs. 309.23 crores for the said 695 days.

(iv) In context of the paragraphs above, it was observed that out of the above 687 days, for 29 days the Company had misused the credit client funds for the settlement obligation of debit balance clients as well as for proprietary purposes. The details of the aforesaid 29 days are tabulated below:

Dates	Aggregate client debit balances as per trial balances (Debtors) (after adjusting for open bills & uncleared cheques)	Aggregate client credit balances as per trial balances (Creditors) (after adjusting for open bills & uncleared cheques}	Total client bank balance	Collaterals deposited with all exchanges by IIFL with supporting documents of exchanges				Total funds available with broker after adjusted 50% of BG [Client bank balances (C) + Collateral with Exchanges Cash+FD +50% BG)]	Broker used credit client fund to debit clients purpose (E=B-F)	Broker used client fund for own purpose (F+A=G)
	Total (In Crs.)	Total (In Crs.)	Total (In Crs.)	BG (In Crs.)	Cash deposit (In Crs.)	FDR (in Crs.)	Total (In Crs.)	Total (In Crs.)	Total (In Crs.)	Total (In Crs.)
	A	B	C	D				E	F	G
30-Jun-2011	238.76	482.80	8.22	363.50	13.11	0.00	376.61	203.08	(279.71)	(40.95)
29-Dec-2011	228.79	474.85	36.76	345.10	10.12	22.50	377.72	241.92	(232.93)	(4.14)
12-Jan-2012	216.19	442.18	7.02	345.10	8.29	32.50	385.89	220.35	(221.82)	(5.64)
19-Jan-2012	237.74	453.24	6.91	325.10	13.29	32.50	370.89	215.25	(237.99)	(0.26)
23-Jan-2012	233.30	477.45	8.50	345.10	8.29	32.50	385.89	221.84	(255.61)	(22.32)
25-Jan-2012	243.98	514.00	10.81	345.10	33.29	32.50	410.89	249.14	(264.85)	(20.88)
30-Jan-2012	250.51	510.46	7.29	345.10	18.29	32.50	395.89	230.63	(279.83)	(29.31)
02-Feb-2012	246.73	500.17	11.53	345.10	25.29	32.50	402.89	241.86	(258.31)	(11.58)
03-Feb-2012	255.13	498.54	12.32	345.10	15.29	32.50	392.89	232.66	(265.88)	(10.75)
06-Feb-2012	253.89	507.24	5.71	345.10	30.29	32.50	407.89	241.05	(266.19)	(12.30)
07-Feb-2012	238.19	515.60	7.56	345.10	22.29	32.50	399.89	234.90	(280.71)	(42.51)
09-Feb-2012	269.26	503.69	5.22	345.10	27.29	28.30	400.69	233.35	(270.34)	(1.08)
IO-Feb-2012	269.34	534.27	9.06	345.10	30.29	28.30	403.69	240.20	(294.07)	(24.72)
14-Feb-2012	265.29	529.55	17.47	345.10	31.09	28.30	404.49	249.41	(280.14)	(14.85)
15-Feb-2012	276.77	538.29	6.42	355.10	34.39	28.30	417.79	246.66	(291.63)	(14.86)
16-Feb-2012	284.82	546.98	-8.28	355.10	56.64	28.30	440.04	254.20	(292.77)	(7.95)
28-Jun-2012	185.68	412.42	4.58	370.10	34.73	0.80	405.63	225.16	(187.26)	(1.58)
20-Sep-2012	176.91	465.31	4.98	485.10	17.18	3.30	505.58	268.02	(197.29)	(20.39)
26-Sep-2012	205.68	492.41	7.27	485.10	28.18	3.30	516.58	281.31	(211.10)	(5.42)

Dates	Aggregate client debit balances as per trial balances (Debtors) (after adjusting for open bills & uncleared cheques)	Aggregate client credit balances as per trial balances (Creditors) (after adjusting for open bills & uncleared cheques}	Total client bank balance	Collaterals deposited with all exchanges by IIFL with supporting documents of exchanges				Total funds available with broker after adjusted 50% of BG [Client bank balances (C) + Collateral with Exchanges Cash+FD +50% BG)]	Broker used credit client fund to debit clients purpose (E=B-F)	Broker used client fund for own purpose (F+A=G)
	Total (In Crs.)	Total (In Crs.)	Total (In Crs.)	BG (In Crs.)	Cash deposit (In Crs.)	FDR (in Crs.)	Total (In Crs.)	Total (In Crs.)	Total (In Crs.)	Total (In Crs.)
	A	B	C	D				E	F	G
08-Oct-2012	221.03	493.37	7.60	445.10	33.68	3.30	482.08	267.14	(226.23)	(5.20)
02-Dec-2013	145.31	431.46	9.38	445.60	6.48	6.85	458.93	245.51	(185.95)	(40.64)
03-Dec-2013	145.96	411.39	15.13	445.60	10.48	6.85	462.93	255.26	(156.13)	(10.17)
04-Dec-2013	142.27	407.58	13.09	445.60	10.48	6.85	462.93	253.21	(154.37)	(12.10)
06-Dec-2013	141.21	396.04	15.89	420.60	10.48	6.85	437.93	243.52	(152.52)	(11.31)
09-Dec-2013	159.55	409.21	13.92	420.60	10.48	6.85	437.93	241.55	(167.66)	(8.11)
IO-Dec-2013	162.55	405.31	12.07	420.60	10.48	6.85	437.93	239.70	(165.61)	(3.06)
II-Dec-2013	170.55	425.67	14.66	420.60	10.48	6.85	437.93	242.29	(183.38)	(12.83)
02-Jan-2014	157.50	400.97	8.62	400.60	20.45	6.85	427.90	236.23	(164.75)	(7.25)
12-May-2014	148.27	436.89	20.20	489.60	16.30	1.65	507.55	282.95	(153.94)	(5.67)

(v) It was observed from the table provided above, that the ledger debit balance of the clients (values in column A) was less than the credit clients fund used for the settlement of debit client obligation (values in column F). The negative value of the "G" column indicates that the Company had utilized client funds for settlement obligation of proprietary trades.

Considering the paragraph above, it was alleged that the Company has contravened provisions of the SEBI 1993 Circular in the following manner: (i) by utilizing funds of credit balance clients for settlement obligation of debit balance clients for 687 days resulting into misutilisation of client funds in the range of Rs 0.58 crores to Rs 309.23 crores; and (ii) by utilizing funds of *credit balance clients for settlement obligation of debit balance clients and proprietary trades for 29 days resulting into misutilisation of client funds in the range of Rs. 0.26 crores to Rs. 42.51 crores.*

8.6 During the inspection, the balance sheet of the Company as on March 31, 2012 was also analyzed and it was observed that out of the total net worth of Rs 1277.28 crores of the Company, Rs 1208.23 crores was invested or utilized by the Company for its group companies. From the above, it was observed that after investing or utilizing the aforesaid amount for its group companies, the Company had only Rs 69.05 crores available as net worth for running its business. Further, it was observed that:

(a) The said net worth was invested in the following asset categories by the Company:

Fixed assets	Rs 26.22 crores
Deferred tax assets	Rs 19.81 crores
Short term loans & advances	Rs 9.92 crores
Current investment	Rs 1.00 crores
Total	**Rs 56.95 crores**

(b) After investing in the asset categories provided above, the Company had Rs 12.1 crores available (*i.e.,* the difference between Rs 69.05 crores and Rs 56.95 crores), which was invested in the following categories of assets:

Long- term loans & advances	Rs 113.02 crores
Other current assets	Rs 116.79 crores
Inventories	Rs 39.22 crores
Total	**Rs 269.03 crores**

8.7 From all the inspections undertaken with respect to Adjudication Proceedings 1 during the period from April 01, 2011 to June 30, 2014, it was observed that IIFL had misused client funds in the range of Rs. 0.59 crores to Rs 397.02 crores in 795 days for settlement obligation of debit balance clients and Rs 0.26 crores to Rs. 73.28 crores in 42 days for proprietary purposes, in addition to the settlement obligation of debit balance clients.

Further, it was also observed that the interest on funds misused by IIFL during the aforesaid period amounted to Rs 34.87 crores.

9. The Company submitted its reply to the SCN *vide* letter dated January 29, 2022. Further, the Noticee submitted its additional submissions *vide* letter dated March 30, 2022. The aforesaid replies of the Noticee have been considered and summarized below for convenience:

9.1 <u>Multiple proceedings initiated against the Noticee</u>

(i) Two enquiry and two adjudication proceedings have been initiated against the Noticee which could have been clubbed together under one comprehensive proceeding.

(ii) Initiation of multiple proceedings in respect of similar observations made in the inspection and supplementary inspections is regulatory overreach, abuse of discretionary power vested with SEBI and perverse action loaded with arbitrariness.

9.2 <u>Enquiry proceedings should not have been initiated in the present matter</u>

(i) The review notings of SEBI shows that the inspection department had only recommended initiation of adjudication proceedings, however, the Whole Time Member decided initiation of enquiry proceedings without any reasoning and justification, which shows that the competent authority was prejudiced while ordering the aforesaid enquiry.

(ii) Imposition of monetary penalty along with recommendation of disciplinary penalty under SEBI (Intermediaries) Regulations (hereinafter referred to as the "**Intermediaries Regulations**") is unwarranted, baseless, excessive and disproportionate.

(iii) In the matter of M/s Motilal Oswal Financial Services Limited, decision dated February 28, 2020, the adjudicating officer had imposed a penalty of Rs 17,00,000 wherein the facts and the allegations were similar to the present case, however, in the said case only adjudication proceedings were initiated. As opposed to that, enquiry as well as adjudication proceedings have been initiated in the present case. Therefore, the Noticee has requested that no recommendation should be made under the Intermediaries Regulations.

9.3 <u>IIFL has not violated provisions of SEBI 1993 Circular</u>

(i) Noticee has been in compliance with applicable circulars at all times in accordance with industry practice. The alleged findings under the SCN does not make a reference to any specific provision of the SEBI 1993 Circular, which shows that the inspection team has not understood the facts of the case and the specific provisions of the SEBI 1993 Circular.

(ii) In support of the above, the Noticee has furnished an analysis in tabular form with respect to compliance with each of the provisions of the SEBI 1993 Circular.

9.4 <u>Non-designation of client bank account as “client account”</u>

(i) The Noticee has submitted that bank accounts at serial nos. 7, 15, 21 and 25 of Annexure II of SCN, have already been closed.

(ii) The bank account at serial no. 6 in Annexure II of SCN is a Citi Bank account and despite several correspondences, Citi Bank was unable to add the suffix “client account”. Therefore, the Noticee has decided to close the account.

(iii) With respect to rest of the 21 accounts, the Noticee has submitted that the said accounts have already been designated as “client account”. The aforesaid accounts have always been exclusively used as client accounts. The Noticee has furnished proof of designation with respect to the aforesaid accounts.

(iv) The SCN itself records that all accounts except 3 accounts were redesignated and were in the process of name change. Thus, there is no failure to designate the bank accounts used for client transactions.

(v) The inspection observation is only with respect to the name of the account and not with respect to any unauthorized use. Therefore, the said observation is only technical and not material in nature.

(vi) As per SEBI circular bearing reference no. SEBI/HO/MIRSD /MIRSD2/CIR/2016/95 dated September 26, 2016 (hereinafter referred to as "**Enhanced Supervision Circular**"), read with NSE, BSE, MCX, NCDEX circular on `Guidelines for maintaining client & settlement bank accounts by the Trading Members' in November 2020, IIFL has rationalized the no. of client bank accounts to below 30 in number and reported all such bank accounts to the exchanges. Further, all client bank accounts are tagged as per nomenclature prescribed by SEBI/exchanges.

9.5 <u>IIFL was following the same practice as the rest of the broking industry with respect to client funds from November 18, 1993 till June 30, 2017</u>

(i) As per the SEBI 1993 Circular, client bank account (pool account) is a dedicated bank account wherein all the client funds through pay-in and pay-outs from the stock exchanges are gathered. From 1993 till the modification effected through the Enhanced Supervision Circular, the entire broking industry including the Noticee had maintained a client funds pool account, into which all client payments received towards pay-in/pay-out to/from stock exchanges settlement accounts were made. The aforesaid is enabled as per clause 1(B) of SEBI 1993 Circular.

(ii) In case of a shortfall in the pool account in meeting the exchange/client obligations, the broker would meet the same through transfer of his own funds, fixed deposits, bank guarantees as and when required, failing which there would be a default on part of the stock broker. The clients usually make pay-in on or before T+2+5 whereas the brokers make payment of margin and pay-in on or before T+2 to stock exchanges. Since the clients have time to make pay-in by T+2, most of the client funds are received from T+2 day onwards, which leads to IIFL deploying its own funds to the extent of shortfall. The shortfall met would then be recovered from the client account.

(iii) In a single consolidated client funds pool account, there is no differentiation between the funds received/paid from/to clients and the stock exchange. All stock brokers, including IIFL, continued to receive funds from debtors/exchange and pay to creditors/exchange on a continuous basis and so the balances were always dynamic in nature.

(iv) The entire broking industry has been following similar practice of monitoring on net creditors basis (*i.e,* total creditors – total debtors) with respect to the funds available in client bank accounts and with stock exchanges.

9.6 Retrospective application of Enhanced Supervision Circular

(i) Law cannot have retrospective application unless the statute provides the same specifically. Under the SEBI Act, SEBI does not have any provision which authorizes it to make regulations or issue circulars which have retrospective application.

(ii) Under the provisions of Enhanced Supervision Circular, SEBI had prescribed the methodology and format of calculation of client fund balances as per the ledger, adjustments thereon and the fund balances available in the client bank accounts, settlement accounts and exchange deposits *etc*. As per the revised SEBI circular, the following modifications were stipulated for calculation of client funds balances which were not present before September, 2016, and therefore, the same was not being practiced by any broker:

(a) Only 50% of the value of bank guarantees would be considered towards fund balances (*i.e.,* only the funded portion); and

(b) Ledger gross credit balances in client accounts would be compared with client bank accounts and stock exchange accounts instead of comparison with the ledger net credit balance.

(iii) Enhanced Supervision Circular which came into effect from July 01, 2017 is not a mere reproduction of the SEBI 1993 Circular as it contains substantial new prescriptions and modifications/clarifications with respect to methodology, calculations, formats, maintenance of accounts, reconciliation, monitoring and reporting *etc.* Enhanced Supervision Circular cannot be made applicable retrospectively against the Noticee when the circular itself states that it shall come into effect prospectively. The Noticee has cited the following two judgments of the Hon'ble Supreme Court in support of the above:

(a) Binani Industries Ltd Kerala vs. Assistant Commissioner of Income Taxes, VI Circle, Bangalore & Ors. (Appeal civil 1784 of 2007), decision dated April 04, 2007; and

(b) SEBI vs. Alliance Finstock Ltd. & Ors. (Civil appeal no. 4493 Of 2006), decision dated November 03, 2015.

(iv) The inspection period pertains to the period beginning from April 01, 2011 to June 2014, and the Enhanced Supervision Circular was made effective from July 01, 2017. By applying the methodology prescribed under the said circular to the aforesaid inspection period, SEBI has attempted to retrospectively apply the provisions of the said circular and levelled charges on the Noticee. The principles and the table provided under the Enhanced Supervision Circular were not made available under the SEBI 1993 Circular. Prior to the Enhanced Supervision Circular, IIFL and the entire broking industry were utilizing client pool account for debit balance clients and the monitoring was done on net client fund basis.

(v) Bank guarantee is considered as cash equivalent upto its full value (without any haircut) by stock exchanges in respect of margin and exposure purposes. Further, stock exchanges have recourse to the full amount of bank guarantee upon invocation in case of any contingency. Therefore, full value of bank guarantee should be considered in calculating the total available funds. The practice that only funded portion of the bank guarantee would be considered was stipulated for the first time in the Enhanced Supervision Circular. However, the calculation made in Supplementary Inspection I, Supplementary Inspection II and Supplementary Inspection III considers 50% of the bank guarantee even though the inspection period is from April 01, 2011 to June, 2014 *i.e,* before the Enhanced Supervision Circular had come into effect. Thus, by considering 50% bank guarantee in its inspection, SEBI has retrospectively applied the norms of Enhanced Supervision Circular.

(vi) The revised working for the 10 days and 105 days identified in Supplementary Inspection I and Supplementary Inspection II wherein it has been alleged that the Company had misused the credit balance of its client funds for pay out obligations of its debit balance clients after taking into account 100% of the bank guarantee and net creditors balance is provided below as follows:

Revised working for 10 days of Supplementary Inspection I

Revised working for 10 days of Supplementary Inspection I										
Date	Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Net creditors	Total of client bank balances	Collateral deposited with all exchanges by IIFL				Total cash available with broker after considering BG @100%	Excess of available cash over net creditors (shortfall)
	A	B	C	D	E			Total	F	G
20-Jun-13	247.44	371.06	123.62	22.62	70.99	3.5	522	596.49	619.11	495.49
21-Jun-13	243.13	337.17	94.04	30.22	70.99	3.5	522	596.49	626.71	532.67
18-Jun-13	199.42	353.83	154.41	15.55	51.99	3.5	522	577.49	593.04	438.63
19-Jun-13	212.84	369.27	156.43	13.4	54.99	3.5	522	580.49	593.89	437.46
24-Jun-13	276.28	326.17	49.89	43.03	70.99	3.5	522	596.49	639.52	589.63
25-Jun-13	264.49	325.05	60.56	25.85	70.99	3.5	522	596.49	622.34	561.78
23-Oct-13	167.05	364.23	197.18	14.46	1.7	6.85	510	518.55	533.01	335.83
24-Oct-13	167.52	352.44	184.92	8.54	1.7	6.85	510	518.55	527.09	342.17
27-Dec-12	180.33	423.26	242.93	27.73	98.34	2.6	505	605.94	633.67	390.74
28-Dec-12	182.24	398.18	215.94	22.72	20.34	2.6	505	527.94	550.66	334.72

Revised working for 105 days of Supplementary Inspection II

Revised working for 105 days of Supplementary Inspection II											
#	Date	Aggregate Clients Debit Balances as per Trial Balance (After adjusting for open bills & uncleared cheques)	Aggregate Clients Credit Balances as per Trial Balance (After adjusting for open bills & uncleared cheques)	Net Creditors	Total of Client Bank Balances	Collateral Deposited with all exchanges by IIFL				Total cash available with broker after considering BG @100%	Excess of available cash over net creditors (Shortfall)
		A	B	C	D	E			Total	F	G
						Cash	FD	BG			
1	10-Mar-14	183.49	337.63	154.14	10.94	12.54	7.65	446.10	466.29	477.24	323.09
2	13-Mar-12	485.20	646.71	161.51	20.25	23.59	28.30	355.10	406.99	427.24	265.72
3	1-Jan-13	163.36	299.54	136.18	12.82	77.84	2.60	505.10	585.54	598.37	462.18
4	6-Jan-12	185.45	407.96	222.51	8.30	35.09	22.50	345.10	402.69	410.98	188.47
5	16-May-14	266.77	462.27	195.50	18.83	75.29	1.65	509.10	586.04	604.87	409.37
6	28-Apr-11	352.63	461.97	109.34	29.29	35.47	-	270.00	305.47	334.76	225.42
7	27-May-14	254.47	541.59	287.12	23.73	30.29	1.65	529.10	561.04	584.77	297.65

Revised working for 105 days of Supplementary Inspection II

#	Date	Aggregate Clients Debit Balances as per Trial Balance (After adjusting for open bills & unclear ed cheques)	Aggregate Clients Credit Balances as per Trial Balance (After adjusting for open bills & unclear ed cheques)	Net Creditors	Total of Client Bank Balances	Collateral Deposited with all exchanges by IIFL				Total cash available with broker after considering BG @100%	Excess of available cash over net creditors (Shortfall)
		A	B	C	D	E			Total	F	G
						Cash	FD	BG			
8	13-Jan-12	200.83	423.78	222.95	8.01	7.09	32.50	345.10	384.69	392.70	169.75
9	8-Aug-11	304.15	476.23	172.08	12.71	3.17	-	350.00	353.17	365.88	193.80
10	26-Dec-11	196.61	405.04	208.43	6.60	7.09	22.50	355.10	384.69	391.29	182.86
11	26-Apr-11	388.46	474.46	86.00	40.61	15.47	-	270.00	285.47	326.08	240.08
12	31-Jan-12	181.77	483.80	302.03	6.62	17.09	32.50	345.10	394.69	401.30	99.27
13	16-Jun-14	253.45	494.51	241.06	28.56	13.29	1.65	538.10	553.04	581.60	340.55
14	18-Apr-11	384.33	486.46	102.13	25.56	36.12	0.87	253.50	290.49	316.05	213.92
15	23-Sep-11	322.89	513.74	190.86	19.13	55.59	-	413.60	469.19	488.32	297.46
16	10-Jun-14	245.96	569.45	323.49	21.55	58.29	1.65	538.10	598.04	619.59	296.09
17	23-Feb-12	253.28	527.59	274.31	10.60	50.59	28.30	355.10	433.99	444.59	170.28
18	11-Apr-14	145.69	375.08	229.39	40.68	20.39	1.65	489.10	511.14	551.82	322.43
19	5-Jul-12	141.09	404.60	263.51	5.92	66.18	0.80	370.10	437.08	443.00	179.49
20	19-May-11	365.95	441.46	75.51	26.91	10.47	-	330.00	340.47	367.38	291.88
21	13-May-14	93.10	386.13	293.04	19.28	40.29	1.65	489.10	531.04	550.32	257.28
22	11-Nov-11	302.75	450.19	147.44	7.97	7.09	27.50	365.10	399.69	407.65	260.21
23	4-Oct-11	277.02	438.65	161.63	11.27	5.59	-	413.60	419.19	430.46	268.83
24	4-May-11	406.19	436.22	30.02	39.06	2.47	-	320.00	322.47	361.53	331.50
25	20-Mar-14	156.86	318.16	161.30	18.11	20.54	7.65	466.10	494.29	512.40	351.10
26	18-Apr-13	169.91	362.95	193.05	18.69	42.99	3.50	532.10	578.59	597.28	404.24
27	12-Mar-13	216.14	327.01	110.87	20.31	17.49	2.50	532.10	552.09	572.40	461.53
28	21-Feb-12	236.34	512.16	275.83	13.02	48.94	28.30	355.10	432.34	445.36	169.53
29	10-Apr-12	181.32	412.17	230.85	7.23	23.59	28.30	345.10	396.99	404.22	173.37
30	26-Mar-12	509.87	362.99	(146.88)	21.84	39.59	28.30	355.10	422.99	444.83	591.71
31	2-May-11	412.13	476.22	64.10	29.00	45.47	-	270.00	315.47	344.47	280.37
32	5-Sep-11	222.81	418.50	195.69	10.43	5.19	10.00	333.60	348.79	359.22	163.53
33	29-Aug-11	254.42	381.64	127.22	10.96	5.09	-	323.60	328.69	339.64	212.42

Revised working for 105 days of Supplementary Inspection II											
#	Date	Aggregate Clients Debit Balances as per Trial Balance (After adjusting for open bills & uncleared cheques)	Aggregate Clients Credit Balances as per Trial Balance (After adjusting for open bills & uncleared cheques)	Net Creditors	Total of Client Bank Balances	Collateral Deposited with all exchanges by IIFL				Total cash available with broker after considering BG @100%	Excess of available cash over net creditors (Shortfall)
		A	B	C	D	E			Total	F	G
						Cash	FD	BG			
34	9-Aug-11	303.65	377.66	74.01	28.77	25.32	-	383.60	408.92	437.69	363.67
35	19-Apr-11	386.31	476.84	90.53	20.96	46.12	0.87	253.50	300.49	321.45	230.92
36	27-Jul-11	289.79	425.12	135.33	9.53	15.61	-	351.70	367.31	376.84	241.51
37	16-Jan-12	209.51	414.33	204.81	8.35	7.09	32.50	345.10	384.69	393.04	188.23
38	13-Sep-11	280.15	452.47	172.32	13.02	29.19	10.00	333.60	372.79	385.80	213.48
39	27-Mar-12	468.37	347.06	(121.31)	17.04	26.59	28.30	355.10	409.99	427.03	548.34
40	12-Sep-11	267.22	449.42	182.20	11.69	18.19	10.00	333.60	361.79	373.48	191.27
41	4-Jul-13	166.37	302.82	136.45	9.73	29.99	3.50	522.10	555.59	565.32	428.86
42	2-Nov-11	255.15	493.63	238.48	6.49	7.09	20.00	365.10	392.19	398.67	160.19
43	20-May-14	298.10	551.26	253.16	20.91	100.29	1.65	509.10	611.04	631.96	378.80
44	21-Jan-13	232.34	390.21	157.87	7.77	13.79	2.60	520.10	536.49	544.27	386.40
45	7-Oct-11	233.27	418.90	185.64	16.58	5.59	-	413.60	419.19	435.77	250.13
46	19-Jun-14	287.13	491.25	204.12	21.84	13.29	1.65	538.10	553.04	574.88	370.77
47	12-Jun-14	313.95	504.53	190.58	32.68	58.29	1.65	538.10	598.04	630.73	440.15
48	13-Dec-11	243.59	422.82	179.23	8.63	7.09	32.50	355.10	394.69	403.32	224.09
49	4-Jul-12	138.36	406.67	268.32	6.02	46.07	0.80	345.10	391.97	397.99	129.67
50	21-Nov-11	336.92	417.03	80.11	26.98	7.09	32.50	365.10	404.69	431.67	351.56
51	11-Apr-11	338.46	535.15	196.69	12.62	36.12	0.87	253.50	290.49	303.10	106.42
52	12-Jul-12	163.42	400.34	236.92	8.76	97.87	0.10	400.10	498.07	506.83	269.91
53	30-Nov-11	176.04	423.40	247.36	7.93	7.09	32.50	345.10	384.69	392.62	145.26
54	24-Nov-11	283.99	455.48	171.49	16.35	7.09	32.50	345.10	384.69	401.04	229.55
55	24-Apr-12	235.74	373.01	137.27	7.29	36.08	28.30	325.10	389.48	396.77	259.50
56	19-Oct-11	285.16	422.71	137.54	9.09	6.59	-	413.60	420.19	429.28	291.73
57	27-Sep-11	232.20	485.18	252.98	12.39	5.59	-	413.60	419.19	431.57	178.59
58	16-Mar-12	517.56	468.58	(48.98)	22.30	20.59	28.30	355.10	403.99	426.29	475.26
59	23-May-13	217.25	441.21	223.97	13.69	34.99	3.50	532.10	570.59	584.29	360.32

Revised working for 105 days of Supplementary Inspection II											
#	Date	Aggregate Clients Debit Balances as per Trial Balance (After adjusting for open bills & uncleared cheques)	Aggregate Clients Credit Balances as per Trial Balance (After adjusting for open bills & uncleared cheques)	Net Creditors	Total of Client Bank Balances	Collateral Deposited with all exchanges by IIFL				Total cash available with broker after considering BG @100%	Excess of available cash over net creditors (Shortfall)
		A	B	C	D	E			Total	F	G
						Cash	FD	BG			
60	13-Feb-12	205.07	512.29	307.22	13.14	29.09	28.30	345.10	402.49	415.62	108.40
61	12-Jun-13	207.41	356.70	149.29	11.63	19.99	3.50	522.10	545.59	557.22	407.93
62	9-May-12	272.21	346.56	74.35	12.05	68.58	13.30	340.10	421.98	434.03	359.68
63	4-Apr-13	150.03	323.47	173.44	14.96	27.49	2.50	532.10	562.09	577.06	403.62
64	25-Jul-13	187.93	349.11	161.18	16.41	54.99	3.50	522.10	580.59	597.00	435.82
65	1-Mar-13	266.12	326.42	60.30	16.33	40.49	2.50	520.10	563.09	579.43	519.13
66	12-Nov-12	196.90	369.25	172.34	33.31	114.09	2.60	465.10	581.79	615.10	442.76
67	9-Dec-11	238.86	446.77	207.91	9.28	7.09	32.50	355.10	394.69	403.97	196.06
68	12-Mar-14	171.85	353.15	181.31	24.61	12.54	7.65	446.10	466.29	490.91	309.60
69	4-Dec-12	205.39	470.52	265.13	13.90	70.84	2.60	495.10	568.54	582.44	317.31
70	7-Aug-13	187.54	305.09	117.54	15.58	17.07	3.50	540.10	560.67	576.26	458.71
71	30-May-14	293.39	521.20	227.81	19.25	14.29	1.65	538.10	554.04	573.29	345.49
72	21-Oct-11	297.82	460.52	162.70	13.76	6.59	-	413.60	420.19	433.95	271.25
73	29-Sep-11	231.97	454.62	222.66	10.54	5.59	-	413.60	419.19	429.73	207.07
74	27-Sep-12	161.20	471.44	310.24	5.69	46.78	2.60	485.10	534.48	540.17	229.93
75	14-Sep-11	289.90	450.22	160.32	13.28	42.19	10.00	333.60	385.79	399.06	238.74
76	19-Aug-13	207.76	324.30	116.54	26.03	19.57	0.50	540.10	560.17	586.20	469.66
77	21-Jul-11	270.93	424.96	154.03	7.48	27.17	-	330.00	357.17	364.65	210.62
78	27-Jul-12	187.97	331.00	143.02	7.27	5.28	0.10	490.10	495.48	502.75	359.73
79	18-Dec-13	175.88	343.67	167.80	14.12	6.39	6.85	400.10	413.34	427.46	259.66
80	15-Dec-11	247.91	402.96	155.05	9.62	7.09	32.50	355.10	394.69	404.30	249.25
81	1-Dec-11	181.09	391.66	210.57	8.85	7.09	32.50	355.10	394.69	403.54	192.97
82	15-Jun-12	155.40	367.97	212.57	8.32	34.33	0.80	370.10	405.23	413.55	200.99
83	9-Jan-12	274.23	415.18	140.95	5.90	7.09	22.50	365.10	394.69	400.58	259.64
84	4-Feb-14	207.98	326.60	118.61	18.17	2.39	6.85	421.10	430.34	448.51	329.90
85	4-Sep-13	195.80	323.34	127.54	11.55	14.56	0.50	528.60	543.66	555.21	427.67

Revised working for 105 days of Supplementary Inspection II											
#	Date	Aggregate Clients Debit Balances as per Trial Balance (After adjusting for open bills & uncleared cheques)	Aggregate Clients Credit Balances as per Trial Balance (After adjusting for open bills & uncleared cheques)	Net Creditors	Total of Client Bank Balances	Collateral Deposited with all exchanges by IIFL				Total cash available with broker after considering BG @100%	Excess of available cash over net creditors (Shortfall)
		A	B	C	D	E			Total	F	G
						Cash	FD	BG			
86	6-May-13	143.39	406.30	262.90	5.32	34.99	3.50	532.10	570.59	575.91	313.01
87	28-Feb-12	286.09	480.54	194.45	9.80	42.09	28.30	355.10	425.49	435.29	240.84
88	23-May-14	306.06	528.30	222.24	21.95	40.29	1.65	519.10	561.04	582.99	360.76
89	28-May-12	218.70	373.32	154.62	8.66	29.58	0.80	370.10	400.48	409.14	254.52
90	19-Dec-11	266.97	400.49	133.52	10.25	7.09	32.50	355.10	394.69	404.94	271.42
91	16-Aug-11	299.36	408.19	108.82	10.53	23.83	-	383.60	407.43	417.96	309.14
92	3-Jan-14	170.56	389.73	219.17	19.76	22.39	6.85	400.10	429.34	449.11	229.94
93	24-Jul-12	172.90	372.81	199.91	8.29	63.02	0.10	490.10	553.22	561.52	361.61
94	25-Oct-12	213.01	428.96	215.95	10.62	22.28	2.60	445.10	469.98	480.60	264.66
95	27-Aug-12	208.64	384.81	176.17	3.87	20.10	2.60	520.10	542.80	546.67	370.50
96	28-Aug-13	212.58	296.24	83.66	15.04	9.56	0.50	540.10	550.16	565.20	481.54
97	4-May-12	237.08	357.37	120.29	24.86	49.58	18.30	325.10	392.98	417.84	297.55
98	5-Oct-11	262.14	432.60	170.47	5.77	5.59	-	413.60	419.19	424.95	254.49
99	19-May-14	246.49	417.49	171.00	21.70	90.29	1.65	509.10	601.04	622.74	451.74
100	17-Jan-13	236.63	410.88	174.25	14.24	22.79	2.60	520.10	545.49	559.73	385.48
101	20-Mar-12	501.16	427.46	(73.70)	11.27	18.59	28.30	355.10	401.99	413.26	486.95
102	28-Sep-12	175.05	444.90	269.85	9.79	44.28	2.60	485.10	531.98	541.78	271.93
103	17-May-12	249.90	351.19	101.29	13.59	53.58	0.80	350.10	404.48	418.08	316.79
104	5-Jul-11	260.80	437.31	176.51	16.92	11.47	-	330.00	341.47	358.39	181.88
105	6-Jun-14	285.67	523.31	237.64	18.32	38.29	1.65	538.10	578.04	596.36	358.73

(vii) Further, similar to the revised working for Supplementary Inspection I and Supplementary Inspection II, the Noticee has furnished revised working for 695 days of Supplementary Inspection III which has been calculated by the Noticee after taking into account 100% of the bank guarantee and net creditors balance.

(viii) Column “G” provided in the revised calculations above demonstrates that there was no shortfall of net creditors balance compared with the balance available in client banks, clearing member and the stock exchanges on any of the identified 810 days (*i.e,* 10 days of Supplementary Inspection I, 105 days of Supplementary Inspection II and 695 days of Supplementary Inspection III). Further, the Noticee denies that there was any negative value in “F” column (*i.e.,* the difference between “E column and “B” column) and hence there was no question of the Noticee utilizing the funds of credit balance clients for settlement obligations of debit balance clients.

(ix) The Noticee has further highlighted that (a) all the debtors of the Noticee were in the normal course of business; (b) the Noticee was fully covered by collaterals of the clients in case of non-receipt of payment from clients; (c) actions as per company policy were undertaken to make the necessary recovery; (d) the Noticee had always issued pay-outs to the clients as per the client requests/settlement periods; (e) no instances have been observed by SEBI and the stock exchanges in the past where Noticee has been unable to make payment to clients on the settlement dates due to insufficient funds; and (f) there has not been any client complaint against the Noticee for denial of limits of fund and securities withdrawal. The above shows that client funds were utilized only for stock exchange settlement purposes or for pay-out to clients which is within the scope of regulations and circulars issued by SEBI and stock exchanges.

(x) When the Enhanced Supervision Circular came into being, the entire broking industry voiced their difficulties in implementing the same as moving from the earlier practice of maintaining a single pool account for routing client funds through pay-ins and payouts of the stock exchanges posed serious challenges. In support of the same, the Noticee has furnished:

(a) Copy of SEBI circular dated December 20, 2016 extending timeline for implementing provisions of Enhanced Supervision Circular;

(b) Copies of press reports regarding the Enhanced Supervision Circular;

(c) Copies of circulars dated June 23, 2017, July 20, 2017, July 28, 2017, September 25, 2017, November 30, 2017 issued by NSE and circulars dated October 17, 2016, October 20, 2016, October 27, 2016, November 22, 2016, December 12, 2016, December 14, 2016, April 26, 2017, May 12, 2017, June 23, 2017, August 29, 2017, September 25, 2017 and November 29, 2017 issued by BSE in relation to Enhanced Supervision Circular.

(xi) Until 2017, there were more than 100 annual inspections, inquiries, visits *etc.* conducted by SEBI/NSE/BSE *etc.* and no adverse interpretation or findings on client funds utilization as alleged in the SCN were communicated to the Company, which shows that SEBI has attempted to retrospectively impose revised methodology prescribed under the Enhanced Supervision Circular.

(xii) In support of the paragraphs above, the Noticee has furnished an analysis in tabular form regarding whether provisions of Enhanced Supervision Circular were reiteration/ modification of provisions of SEBI 1993 Circular or whether they were new provisions. The analysis concludes that that the principles and formats provided under the Enhanced Supervision Circular were new provisions which were not provided under the SEBI 1993 Circular.

(xiii) The review findings of SEBI in the note mentioning about the alleged findings of segregation of funds and utilization of client funds *etc.* is based on its own hypothesis without taking into account the extant circular and the systems and process followed by the broking industry and IIFL at that time.

9.7 <u>IIFL has not used client bank account for own purposes *viz.* investment/expenses as alleged in Comprehensive Inspection</u>

(i) As explained in the revised workings tabulated above, the Noticee had surplus funds available with the stock exchanges/pool accounts in respect of transactions mentioned in 8.2(vi)(b) above. With respect to mutual funds, the Company has submitted that day to day surplus in bank accounts were parked on overnight basis in money market instruments, which were eventually used for stock exchange/settlement purposes. Thus, the Company had not used client funds for its own use.

(ii) From 2014 onwards, the Noticee has implemented process level changes to ensure seamless flow of funds from/to client accounts and from/to stock exchange accounts along with discontinuation of proprietary trading, as summarized below:

(a) With effect from April 2014, the Company had segregated its proprietary trading into separate membership namely 5paisa Capital Limited (formerly IIFL Capital Limited). Therefore, from April 2014 onwards, the Company was neither undertaking proprietary trading nor there were any instances of pay-in/pay out of positions towards proprietary positions.

(b) It has implemented withdrawal of own funds towards brokerage charges, depository charges *etc* from the client pool account to Noticee’s account on fortnightly basis.

(c) With a view to segregate the broking business from investment banking and own investments in subsidiaries, with effect from February, 2014, the Noticee had restructured the holding company whereby the broking business was demerged into a 100% subsidiary with the name India Infoline Ltd. and the holding company as IIFL Holdings Ltd.

(d) It has streamlined the process of pool account balance reconciliation and have implemented a system based tracking and maintenance of balances in client bank accounts to ensure that the net credit balances of client accounts are maintained in the client bank accounts and with the stock on a daily basis.

(e) Under the revised system:

(e.1) The Noticee is maintaining separate bank accounts for pooling client funds with Citi Bank account no. 9335 and ICICI Bank account no. 917 whereas for its own funds, separate bank accounts are maintained with Citi Bank Pool Account, ICICI Bank Pool Account and ICICI Bank account no. 74198.

(e.2) The aforesaid accounts are separate from own bank accounts from where any shortfall in clients pay-in are made. This ensures that the pool accounts are maintained only for pay-in and pay-out of client funds and its own funds are transferred from/to separate bank account.

(e.3) Withdrawal of brokerage levies and other charges from the pool account to its own account is effected on fortnightly basis.

9.8 <u>Noticee has not used the client funds for own purposes or settlement obligation of proprietary trades as alleged in Supplementary Inspection II and III</u>

(i) It has been alleged in the SCN that it was observed during Supplementary Inspection II that out of the identified 101 days, for 13 days, IIFL had used the client funds for settlement obligation of proprietary trades which led to misutilisation ranging from Rs 2.02 crores to Rs 73.28 crores.

(ii) SEBI 1993 Circular provides the purposes for which money can be drawn from the client accounts but does not provide the manner of calculation or adjustment or methodology for arriving at client balances as per brokers' ledger account with that of client balances in the bank account, exchange balances, value of bank guarantee *etc.*

(iii) During the years 2011 to 2014, the net worth of IIFL was over Rs. 1200 crores. Further, it had net worth of Rs. 1310 crores as on March 31, 2013. The Company has always kept Rs. 400 to Rs. 600 crores of its own funds with the stock exchanges/clients pool accounts to meet its obligation as well as to meet shortfall, if any, in the client accounts. The Company always ensured upfront payment of margins as well as advance pay-ins were made to the stock exchanges *etc.* out of its own surplus funds kept in the client pool accounts or stock exchanges at any point of time which was debited in the clients ledger at end of day. The Company had also paid the value at risk (VaR) and exposure margin on client trades to the stock exchanges upfront which were later collected from clients in the form of funds and/or securities which has not been considered during inspection. Further, the aggregate value of collaterals deposited with clearing corporation in the form of fixed deposits does not take into account the deposits made with the exchanges towards disputed clients, arbitration claims *etc.*

(iv) The revised calculation of the funds available for the said 13 days of Supplementary Inspection II and the excess cash available after payment of proprietary obligation is tabulated below as follows:

Revised calculation of 13 days of Supplementary Inspection II

Date	Aggregate clients debit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Aggregate clients credit balances as per trial balance (after adjusting for open bills & uncleared cheques)	Net creditors	Total of client bank balances	Collateral deposited with all exchanges by IIFL				Total cash available with broker after considering BG @100%	excess of available cash over net creditors (short fall)	Prop. obligation {(+) payout/(-) pay-in}	Excess of available cash over after prop. obligation
	A	**B**	**C**	**D**	**E**			**Total**	**F**	**G**	**H**	**I**
					Cash	**FD**	**BG**					
13-Jan-12	200.83	423.78	222.95	8.01	7.09	32.50	345.10	384.69	392.70	169.75	-	**169.75**
31-Jan-12	181.77	483.80	302.03	6.62	17.09	32.50	345.10	394.69	401.30	99.27	-	**99.27**
23-Feb-12	253.28	527.59	274.31	10.60	50.59	28.30	355.10	433.99	444.59	170.28	-	**170.28**
5-Jul-12	141.09	404.60	263.51	5.92	66.18	0.80	370.10	437.08	443.00	179.49	7.48	**186.97**
21-Feb-12	236.34	512.16	275.83	13.02	48.94	28.30	355.10	432.34	445.36	169.53	-	**169.53**
5-Sep-11	222.81	418.50	195.69	10.43	5.19	10.00	333.60	348.79	359.22	163.53	-	**163.53**
2-Nov-11	255.15	493.63	238.48	6.49	7.09	20.00	365.10	392.19	398.67	160.19	-	**160.19**
4-Jul-12	138.36	406.67	268.32	6.02	46.07	0.80	345.10	391.97	397.99	129.67	(0.95)	**128.72**
11-Apr-11	338.46	535.15	196.69	12.62	36.12	0.87	253.50	290.49	303.10	106.42	-	**106.42**
30-Nov-11	176.04	423.40	247.36	7.93	7.09	32.50	345.10	384.69	392.62	145.26	-	**145.26**
27-Sep-11	232.20	485.18	252.98	12.39	5.59	-	413.60	419.19	431.57	178.59	-	**178.59**
13-Feb-12	205.07	512.29	307.22	13.14	29.09	28.30	345.10	402.49	415.62	108.40	-	**108.40**
27-Sep-12	161.20	471.44	310.24	5.69	46.78	2.60	485.10	534.48	540.17	229.93	(1.36)	**228.57**

(v) Similarly, the revised calculation of the funds available for the 29 days of the Supplementary Inspection III and the excess cash available after payment of proprietary obligation is tabulated below as follows:

Revised calculation of 29 days of Supplementary Inspection III												
Dates	**Aggregate client debit balances as per trial balance (debtors) (after adjusting for open bills & uncleared cheques}**	**Aggregate client credit balances as per trial balance (creditors) (after adjusting for open bills & uncleared cheques}**	**Net creditors**	**Total client bank balance**	**Collaterals deposited with all exchanges by IIFL with supporting documents of exchanges**				**Total cash available with broker after considering BG @100 %**	**Excess of available cash over net creditors (shortfall)**	**Prop. obligation {(+) payout /(-) pay-in}**	**Excess of available cash over after prop. obligation**
	Total (In Crs.)	**Total (In Crs.)**		**Total (In Crs.)**	**BG (In Crs.**	**Cash deposit (In Crs.)**	**FDR (In crs)**	**Total (In Crs.)**				
	A	**B**	**C**	**D**	**E**				**F**	**G**	**H**	**I**
30-Jun-2011	238.76	482.80	244.04	8.22	363.50	13.11	0.00	376.61	384.83	140.80	0.00	140.80
29-Dec-2011	228.79	474.85	246.06	36.76	345.10	10.12	22.50	377.72	414.47	168.41	0.00	168.41
12-Jan-2012	216.19	442.18	225.99	7.02	345.10	8.29	32.50	385.89	392.90	166.91	0.00	166.91
19-Jan-2012	237.74	453.24	215.50	6.91	325.10	13.29	32.50	370.89	377.80	162.29	0.00	162.29
23-Jan-2012	233.30	477.45	244.16	8.50	345.10	8.29	32.50	385.89	394.39	150.23	0.00	150.23
25-Jan-2012	243.98	514.00	270.02	10.81	345.10	33.29	32.50	410.89	421.69	151.67	0.00	151.67
30-Jan-2012	250.51	510.46	259.94	7.29	345.10	18.29	32.50	395.89	403.18	143.24	0.00	143.24
02-Feb-2012	246.73	500.17	253.44	11.53	345.10	25.29	32.50	402.89	414.41	160.97	0.00	160.97
03-Feb-2012	255.13	498.54	243.41	12.32	345.10	15.29	32.50	392.89	405.21	161.80	0.00	161.80
06-Feb-2012	253.89	507.24	253.34	5.71	345.10	30.29	32.50	407.89	413.60	160.25	0.00	160.25
07-Feb-2012	238.19	515.60	277.41	7.56	345.10	22.29	32.50	399.89	407.45	130.04	0.00	130.04
09-Feb-2012	269.26	503.69	234.43	5.22	345.10	27.29	28.30	400.69	405.90	171.47	0.00	171.47
10-Feb-2012	269.34	534.27	264.92	9.06	345.10	30.29	28.30	403.69	412.75	147.83	0.00	147.83
14-Feb-2012	265.29	529.55	264.26	17.47	345.10	31.09	28.30	404.49	421.96	157.70	0.00	157.70
15-Feb-2012	276.77	538.29	261.51	6.42	355.10	34.39	28.30	417.79	424.21	162.69	0.00	162.69
16-Feb-2012	284.82	546.98	262.16	-8.28	355.10	56.64	28.30	440.04	431.75	169.60	0.00	169.60
28-Jun-2012	185.68	412.42	226.74	4.58	370.10	34.73	0.80	405.63	410.21	183.47	-3.06	180.41
20-Sep-2012	176.91	465.31	288.40	4.98	485.10	17.18	3.30	505.58	510.57	222.16	4.79	226.95
26-Sep-2012	205.68	492.41	286.72	7.27	485.10	28.18	3.30	516.58	523.86	237.13	5.11	242.24
08-Oct-2012	221.03	493.37	272.33	7.60	445.10	33.68	3.30	482.08	489.69	217.35	3.54	220.89
02-Dec-2013	145.31	431.46	286.15	9.38	445.60	6.48	6.85	458.93	468.31	182.16	2.01	184.17
03-Dec-2013	145.96	411.39	265.43	15.13	445.60	10.48	6.85	462.93	478.06	212.63	0.86	213.49

Revised calculation of 29 days of Supplementary Inspection III												
Dates	**Aggregate client debit balances as per trial balance (debtors) (after adjusting for open bills & uncleared cheques}**	**Aggregate client credit balances as per trial balance (creditors) (after adjusting for open bills & uncleared cheques}**	**Net creditors**	**Total client bank balance**	**Collaterals deposited with all exchanges by IIFL with supporting documents of exchanges**				**Total cash available with broker after considering BG @100 %**	**Excess of available cash over net creditors (shortfall)**	**Prop. obligation {(+) pay out /(-) pay-in}**	**Excess of available cash over after prop. obligation**
	Total (In Crs.)	**Total (In Crs.)**		**Total (In Crs.)**	**BG (In Crs.**	**Cash deposit (In Crs.)**	**FDR (In crs)**	**Total (In Crs.)**				
	A	**B**	**C**	**D**	**E**				**F**	**G**	**H**	**I**
04-Dec-2013	142.27	407.58	265.31	13.09	445.60	10.48	6.85	462.93	476.01	210.70	-1.05	209.65
06-Dec-2013	141.21	396.04	254.82	15.89	420.60	10.48	6.85	437.93	453.82	198.99	0.19	199.18
09-Dec-2013	159.55	409.21	249.66	13.92	420.60	10.48	6.85	437.93	451.85	202.19	-3.17	199.02
10-Dec-2013	162.55	405.31	242.76	12.07	420.60	10.48	6.85	437.93	450.00	207.24	0.60	207.84
11-Dec-2013	170.55	425.67	255.11	14.66	420.60	10.48	6.85	437.93	452.59	197.47	0.93	198.40
02-Jan-2014	157.50	400.97	243.47	8.62	400.60	20.45	6.85	427.90	436.53	193.05	0.00	193.05
12-May-2014	148.27	436.89	288.62	20.20	489.60	16.30	1.65	507.55	527.75	239.13	0.00	239.13

(vi) It can be seen from the aforesaid tables that the Noticee had surplus funds available with the stock exchanges/pool accounts and the same were utilized towards proprietary obligation. Thus, the Company had not used client funds for settlement obligation of proprietary accounts.

(vii) With effect from April 2014, the Company had segregated its proprietary trading into separate membership namely 5paisa Capital Limited (formerly IIFL Capital Limited). Therefore, from April 2014 onwards, the Company was neither undertaking proprietary trading nor there were any instances of pay-in/pay out of positions towards proprietary positions.

9.9 <u>The Noticee had sufficient net worth at all times</u>

(i) The Noticee's net-worth did not go below the prescribed limits at any point of time. The audited net worth certificate was submitted to NSE, BSE *etc.* periodically (half yearly) and with SEBI as and when required.

(ii) There have been no adverse findings or observations from the stock exchanges/SEBI.

(iii) In support of the above, the Noticee has provided a copy of net worth certificate dated May 22, 2013.

9.10 <u>No adverse findings with respect to segregation of client funds or utilization of client funds were recorded by NSE and BSE in the report submitted by them to IIFL pursuant to Comprehensive Inspection</u>

(i) The SCN was issued pursuant to a joint inspection carried out by SEBI, NSE and BSE in August, 2014. Based on the same joint inspection, NSE had separately sent the inspection report covering the observations of NSE and BSE to IIFL *vide* letter dated January 15, 2015.

(ii) The inspection report of NSE and BSE does not record any adverse observations regarding the segregation of client funds, pay-in and pay-out of client funds, verification of control accounts, verification of routing of client funds in bank books and cross verified with bank statements *etc.* Further, the report sent by NSE in paragraph no 1.14 clearly confirms that third party funding/transaction were not observed by NSE and BSE. Further, it also clearly observed that no irregularities were observed in pay-in/pay-out of funds and securities of clients and client funding through NBFC arm.

(iii) NSE had issued action taken report dated October 16, 2015 which did not contain any major violations and concluded the same with levy of Rs. 11,000 penalty which was debited to IIFL's account. Similarly, BSE had also issued an action taken letter dated July 14, 2015 with no adverse observations and concluded with levy of Rs.10,000 penalty which was debited to IIFL's account.

(iv) The SCN, copy of the inspection of documents given by SEBI, and the review of inspection report sent by SEBI to BSE and NSE *vide* letter dated June 04, 2015 shows that SEBI has not taken into account inspection findings of NSE and BSE, the action taken report, penalties and conclusion of actions.

9.11 <u>There was no misutilisation of client funds, therefore, the question of ill-gotten gains does not arise</u>

(i) The Noticee has denied the allegation that it has illegally gained Rs. 34.87 crs by misusing client funds as it had its own surplus funds available.

(ii) There is nothing placed on record to ascertain the actual disproportionate gain or unfair advantage alleged in the SCN. The amount of Rs. 34.87 crores arrived at by SEBI is a notional figure after considering hypothetical interest rates assuming that borrowing would be required to fund debit balances.

9.12 Similar breaches in the following cases were held by SEBI as technical lapses not warranting substantive punishment. SEBI had only served a letter of warning in the following cases:

(i) Order passed by the Whole Time Member in the matter of M/s. J. M. Morgan Stanley Retail Services Pvt. Ltd. dated June 02, 2004.

(ii) Order passed by Chairman in the matter of M/s. Bama Securities Ltd. dated June 04, 2004.

(iii) Order passed by Whole Time Member in the matter of M/s. Bakliwal Investment dated May 18, 2004.

(iv) Order passed by Whole Time Member in the matter of Twenty First Century Shares and Securities Limited dated December 30, 2005.

(v) Order passed by Whole Time Member in the matter of Mahesh Kothari Share and Stock Brokers Pvt. Ltd. dated October 08, 2012.

Further, the Noticee has submitted that Hon'ble SAT in the matter of Chona Financial Services Pvt. Limited dated August 23, 2004, modified penalty to a warning with respect to an appellant who was *inter alia* charged with the allegation of non-segregation of client's fund and misutilization of client account.

9.13 Noticee has fully implemented the system prescribed under the Enhanced Supervision Circular. In support of the above, the Noticee has furnished copies of compliances and reporting of balances for July, 2017. Thus, the holistic purpose of inspection and rectification action has been complied by IIFL. Noticee has further relied on the following orders wherein Hon'ble SAT had noted the prompt rectification or implementation and dropped the proceedings:

(i) Order in the matter of M/s. DSE Financial Services Ltd. (Appeal no. 153 of 2012) dated September 11, 2012.

(ii) Order in the matter of UPSE Securities Limited vs. SEBI (Appeal no. 109 of 2011) dated July 25, 2011.

9.14 Lastly, the Noticee has submitted that the following adjudication orders should be taken into account which have similar facts and allegations as the present case and where minimal penalties were imposed by the adjudicating officer:

S.No	Adjudication order details
1.	Bearing reference no. Order/SS/VS/2019-20/5169 in the matter of Allvin Securities Limited dated October 24, 2019
2.	Bearing reference no. Order/SS/SK/2019-20/5168 in the matter of SPFL Securities Limited dated October 24, 2019
3.	Bearing reference no. EAD/BD/BM/2019-20/5284 in the matter of M/s Paterson Securities Private Limited dated October 31, 2019.
4.	Bearing reference no. EAD/ BJD/VS/2018-19/1581 in the matter of M/s Anand Rathi Share and Stock Brokers Limited dated November 27, 2018.
5.	Bearing reference no. EAD-2/DSR/RG/ 319/2014 in the matter of Keynote Capital Limited dated December 18, 2014.
6.	Bearing reference no. Order/PM/NK/2019-20/6988 in the matter of M/s Motilal Oswal Financial Services Limited dated February 28, 2020.
7.	Bearing reference no. Order/PM/NK/2019-20/6989] in the matter of M/s Nirmal Bang Securities Private Limited dated February 28, 2020.
8.	Bearing reference no. SD/AO/36/2011 in respect of M/s Mansukh Securities and Finance Limited dated November 02, 2011.
9.	Bearing reference no. Order/PM/NK/2018-19/1778 in respect of M/s Bikash Sureka dated December 28, 2018.
10.	Bearing reference no. RA/CB/381/2018 in respect of M/s Dani Shares and Stocks Pvt. Limited dated May 09, 2018.
11.	Bearing reference no. Order/AA/AR/2019-20/6314 in respect of Satco Capital Markets Ltd dated December 30, 2019.
12.	Bearing reference no. PM/AO/NK-13/2017 in respect of M/s Systematix Shares & Stocks (I) Limited dated December 20, 2017.
13.	Bearing reference no. Order/SM/AR/2018-19/667 in respect of Yoke Securities Ltd. dated May 30, 2018.

10. *Vide* email sent on November 22, 2021, the Noticee requested inspection of certain documents in relation to Adjudication Proceedings 1. *Vide* email sent on January 06, 2022., the Noticee was *inter alia* informed that inspection of an intermediary is an interactive process wherein the inspection team visits the intermediary and collects the data or requests for data through emails (as the situation warrants), analyses the said data and prepares inspection report. The findings of the said inspection report after approval of the competent authority is shared with the concerned intermediary for providing explanations/comments on the inspection findings from the inspection report. Thereafter, depending on the gravity of the misconduct, the inspection team either accepts the explanations/comments to the inspection findings provided by the intermediary and recommends no action or rejects the explanation/comments to the inspection findings provided by the intermediary and recommends action. Thus, the Noticee is considered to be

well-versed with the documents which have been relied upon in the SCN as the same are arising from the aforesaid process. In light of the above, the Noticee was informed that the documents provided to it along with the SCN are sufficient for it to submit a reply in line with the principles of natural justice. *Vide* the same email, the Noticee was granted a hearing opportunity on January 13, 2022.

11. *Vide* email sent on January 06, 2022, the Noticee again requested for inspection of documents along with request for rescheduling the aforesaid hearing granted. *Vide* email sent on January 08, 2022, the Noticee was informed that no additional facts or documents have been brought on record since the last email was sent by the undersigned which would make the undersigned deviate from its earlier stance. The Noticee was informed again that the documents requested for inspection are documents which either have been provided by it or prepared based on the data provide by it, thus, the Noticee is well aware of its contents for submitting an efficacious reply. Further, taking into account the reasons cited by the Noticee for rescheduling the hearing, the Noticee was informed that the hearing date is postponed to a date which shall be intimated subsequently.

12. *Vide* notice of hearing sent *vide* email on February 18, 2022, the Noticee was granted a hearing opportunity on February 25, 2022. *Vide* email sent on February 21, 2022, the authorized representatives of the Noticee (hereinafter referred to as "**ARs**") requested for adjournment of the aforesaid hearing due to unavailability of their counsel. Therefore, the hearing granted on February 25, 2022 was rescheduled to March 14, 2022. In view of COVID-19, the hearing was scheduled through video conferencing on cisco webex platform. On March 14, 2022, the hearing was conducted wherein the ARs appeared before me through video conference and reiterated the submissions made by the Noticee *vide* letter dated January 29, 2022 with respect to Adjudication Proceedings 1. Further, the ARs sought further time till March 21, 2022 for making additional submissions, which was acceded to. As stated before, the

Noticee submitted its additional submissions *vide* letter dated March 30, 2022.

D. CONSIDERATION OF ISSUES AND FINDINGS

7. After considering the facts of the case, I find that the issues that arise for consideration in the instant matter are as follows:

   I. **Issue No. I**: Whether the Noticee has violated the provisions of the SEBI 1993 Circular?

   II. **Issue No. II**: If yes, whether the violation, on the part of the Noticee would attract monetary penalty under section 23D of SCRA?

   III. **Issue No. III**: If the answer to Issue No. II is in affirmative, what would be the monetary penalty that can be imposed upon the Noticee taking into consideration the factors stipulated in section 23J of SCRA read with rule 5(2) of SCRA Adjudication Rules?

8. Before beginning with the contentions raised by the Noticee on merits, I find it appropriate to address three preliminary contentions raised by the Noticee. *First* preliminary contention is that initiation of two enquiry and two adjudication proceedings against the Noticee is perverse, as the aforesaid proceedings could have been clubbed under one comprehensive proceeding. In this regard, as tabulated in paragraph 3 above, total of six inspections were conducted with respect to the affairs of the Noticee. The inspection period with respect to five out of the six inspections pertains to the period from April 01, 2011 to June 30, 2014. The said five inspections are namely, Thematic Inspection, Comprehensive Inspection, Supplementary Inspection I, Supplementary Inspection II and Supplementary Inspection III. As stated before, the allegations arising from the findings of the aforesaid five inspections are clubbed under Adjudication Proceedings 1, and the allegations arising out of the inspection period pertaining to the period from

April 01, 2015 to January 31, 2017 (*i.e*, March 2017 Inspection), is covered under Adjudication Proceedings 2. As regards the two enquiry proceedings, the first enquiry proceedings were initiated based on the findings of the Thematic Inspection, the Comprehensive Inspection, Supplementary Inspection I and Supplementary Inspection II, pursuant to which a SCN dated May 02, 2017 was issued. Thereafter, Supplementary Inspection III and the March 2017 Inspection was conducted, therefore, the aforesaid two inspections form part of the second enquiry proceedings. Taking into account the aforesaid, I find that initiation of two separate adjudication proceedings is justified on the ground of different inspection periods, and initiation of two separate enquiry proceedings is justified due to the subsequent inspections undertaken.

9. *Second*, the Noticee has contended that the Whole Time Member was prejudiced in ordering initiation of enquiry proceedings without justification when the inspection team had recommended initiating adjudication proceedings against the Noticee. I note from internal notings that it has been explicitly recorded by the competent authority that "*given the nature of violations being grievous, more severe action in terms of <u>adjudication and enquiry</u> should be initiated against the broker*". Further, I find that the review notings being referred to by the Noticee dated January 04, 2017 records that *"<u>detailed presentation was made to WTM</u>…..It was decided that <u>enquiry proceedings may be initiated</u> against M/s. India Infoline Limited immediately".* In light of the fact that the Whole Time Member was fully apprised of the alleged violations found by the inspection team against the Noticee, I do not agree with the Noticee's contention that the Whole Time Member was prejudiced while ordering initiation of enquiry proceedings.

10. *Third*, the Noticee has argued that imposition of penalty under adjudication proceedings along with recommendation of disciplinary action under enquiry proceedings is baseless and excessive. The Noticee has cited the decision of adjudicating officer in the matter of M/s Motilal Oswal Financial Services Limited, decision dated February 28, 2020, wherein according to the Noticee,

on similar set of facts, only adjudication proceeding was initiated. In this regard, I find that the correct position has been aptly summarized by Hon'ble Securities Appellate Tribunal, in the case of ***Grishma Securities Private Limited and Ors. vs. SEBI*** (Appeal No. 151 of 2013) dated October 28, 2013. In this case it was argued by the appellant that initiation of adjudication and enquiry proceedings on the same set of facts and evidence is impermissible in law. In context of the above, Hon'ble SAT held the following:

"It is pertinently noted that the adjudication proceedings may lead to monetary penalty or even exoneration of the appellants. Whereas, the enquiry proceedings have the potential of leading to appropriate disciplinary action against the appellants in case the charges are proved in the enquiry. <u>There is no categorical challenge to such parallel proceedings</u>…….

……Once an Inquiry Officer or an Adjudicating Officer is appointed as per law to conduct an enquiry into the alleged misconduct of a company or a market player, as the case may be, he or she acts as an independent, neutral and impartial umpire despite being on the rolls of the SEBI. As long as he holds such responsibility, he or she is supposed to perform a quasi-judicial task dispassionately. However, he or she has to conform to the principles of natural justice and also discharge the said functions within the parameters prescribed by the rules and regulations or an Act of Parliament failing which alone his or her findings or conduct may be questioned and not otherwise.

<u>Therefore, keeping in view the scheme of the SEBI Act, 1992, we have no hesitation in holding that a subjective decision as to when and where regulatory intervention is required is the sole prerogative of the regulator. Undoubtedly, such a decision has to be rational and is to be based on a prima facie and bonafide satisfaction as to the existence of certain alleged irregular or illegal facts/happenings or circumstances supposedly taking place or prevailing in the affairs of a company</u>….." (emphasis supplied)

Considering the above, I find that it is the exclusive right of SEBI to decide which proceedings should be initiated in a particular matter. Thus, the preliminary contentions of the Noticee deserve to be rejected.

I. Issue No. I: Whether the Noticee has violated the provisions of the SEBI 1993 Circular?

11. It is alleged in the SCN that the Noticee has violated the provisions of the SEBI 1993 Circular, for convenience, the relevant extracts are provided below:

__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.

<u>A] Member Broker to keep Accounts:</u> 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.

<u>B] Obligation to pay money into "clients accounts".</u> 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).

<u>C] What moneys to be paid into "clients account".</u> 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.

<u>D] What moneys to be withdrawn from "clients account".</u> 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 above.

<u>E] Right to lien, set-off etc., not affected</u>. 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.

***2.** It shall be compulsory for all Member brokers to keep separate accounts for client's securities and to keep such books of accounts, as may be necessary, to distinguish such securities from his/their own securities. Such accounts for client's securities shall, inter-alia provide for the following:-*

a. Securities received for sale or kept pending delivery in the market;

b. Securities fully paid for, pending delivery to clients;

c. Securities received for transfer or sent for transfer by the Member, in the name of client or his nominee(s);

d. Securities that are fully paid for and are held in custody by the Member as security/margin etc. Proper authorization from client for the same shall be obtained by Member;

e. Fully paid for client's securities registered in the name of Member, if any, towards margin requirements etc;

f. Securities given on Vyaj-badla. Member shall obtain authorization from clients for the same.

Allegation levelled in the Thematic Inspection

12. I find it appropriate to chronologically deal with the allegations levelled in the present matter. It is alleged in the Thematic Inspection as provided in paragraph 8.1 above, that the Noticee has not designated 3 client bank accounts as "client account" in violation of the provisions of SEBI 1993 Circular. The Noticee has provided proof of designation of 21 client bank accounts. After analysing the documents furnished by the Noticee, my findings with respect to the said 3 client accounts are examined in detail below.

13. The said 3 bank accounts not designated as "client accounts" by the Noticee are as follows:

Reference	**Account no.**	**Bank name**
Serial no. 12 of Annexure III to SCN	857764118	Citi Bank
Serial no. 17 of Annexure III to SCN	00820100012078	DCB Bank Ltd.
Serial nos. 39 of Annexure III to SCN	25073000002308	South Indian bank

14. I note that the Noticee in its reply has submitted that the Citi Bank account bearing number 857764118 has been closed. In relation to the aforesaid account, the Noticee has provided a screenshot (page 189 of the annexures to reply) which states "*Welcome Upendra Jaiswal*" and the login date reflected in the screenshot is "*05th October 2017*". I am unable to understand

the purpose of providing the said screenshot in evidence if the Noticee is claiming that the said account has been closed. On the contrary, in absence of any evidence which confirms that the said account is closed, I find that the screenshot suggests that the account has not been closed and it has not been redesignated as well. Further, with respect to account with DCB Bank Ltd. bearing number 00820100012078, the Noticee has submitted that it has designated it as a "client account". In support of the above, the Noticee has furnished a copy of bank confirmation letter addressed by DCB Bank Ltd. to the Noticee dated January 04, 2017 (page 172 of annexures to reply) which provides the balance of "*India Infoline Ltd. - Client A/c*" as on December 31, 2016. Thus, I find that the Noticee has appropriately designated the aforesaid client bank account. As regards account no. 25073000002308 with South Indian Bank, the Noticee has not submitted any explanation in its reply regarding the status of its designation. In this regard, I find that clause 1(B) of the SEBI 1993 Circular clearly states that every member broker is required to pay money to an account kept in the name of the member wherein the title should include the word "client".

15. If I were to accept that the Noticee has genuinely closed the aforesaid Citi Bank account even though no proof has been placed before me, I find that Noticee would still be in violation of clause 1(B) of the SEBI 1993 Circular by not designating account no. 25073000002308 held with South Indian Bank as "client account".

16. The Noticee has also submitted that the aforesaid violation is technical in nature as the said inspection observation is only with respect to the account name and not unauthorized use. I do not subscribe to the Noticee's view. I find that designating client accounts as "client account" is the first step to ensure that there is no unauthorized use. If there is any ambiguity relating to whether any account is client account or not, there is a probability of client funds being mixed with other funds. If the accounts have been designated as "client account", it would be easier to ascertain if the transactions from the accounts are exclusively related to clients or not. Thus, I find that designating

relevant accounts as “client account” serves an important purpose which cannot be termed as “technical” in nature.

17. The Noticee has also submitted that it has rationalized the no. of client bank accounts *inter alia* in compliance with the Enhanced Supervision Circular. It is pertinent to highlight here that during the Thematic Inspection it was observed that the Noticee has not designated 26 client accounts as “client account”, which was informed to the Company. Thereafter, the Company informed SEBI *vide* its letter dated July 11, 2014, that it had submitted the request to its bankers for changing the title of the aforesaid 26 client accounts to “client account” and provided supporting document which contained status of 45 bank accounts. The Company also informed SEBI that out of the 45 client accounts examined most of the client accounts have been designated as client account. On perusal of the aforesaid supporting document, it was observed that 3 client bank accounts were still in the process of changing the title to “client bank account”, therefore, the SCN was issued containing the allegation that the Noticee has not designated 3 accounts as “client accounts”. After providing the status of the designation of client bank accounts *vide* the aforesaid letter (*i.e,* July 11, 2014), the Noticee had an opportunity on receiving the SCN to place satisfactory evidence regarding the status of 3 accounts, however, as noted above, it has failed to place appropriate evidence with respect to 2 out of the 3 accounts. Thus, I find that taking shelter under the garb of compliance with the Enhanced Supervision Circular does not help the case of the Noticee as *firstly*, the Noticee had sufficient time to comply with the provisions of the SEBI 1993 Circular, and *secondly*, the allegation is with respect to the violation of SEBI 1993 Circular and not the Enhanced Supervision Circular and/or extant regulations/circular.

<u>Allegations levelled in the Comprehensive Inspection</u>

18. Moving on to the allegations levelled in the Comprehensive Inspection, I note from the Comprehensive Inspection that with respect to settlement of funds,

the Noticee had submitted that funds are transferred from client accounts as well as its own accounts to pool accounts, and from the pool accounts, the funds are transferred to the control account. Subsequently, from the control account, the money is finally transferred to the stock exchange settlement account.

19. I note that the SCN alleges that client funds were transferred from client accounts to Citi Bank Pool Account, Axis Bank Pool Account, ICICI Bank Pool Account and HDFC Bank Pool Account and the aforesaid pool accounts were also used for own purposes of IIFL such as investment in mutual funds, transfers to group companies, foreign remittance expenses *etc*. I find that the Noticee in its reply has claimed that as the Noticee had its own surplus available with the stock exchanges/clients pool account, it had not used the client funds lying in the pool accounts. I find that the aforesaid reply of the Noticee is evasive as it does not address the specific allegations levelled against it. The allegation levelled against the Noticee in the SCN is that the same account was used for clients as well as its own purposes which falls foul of SEBI 1993 Circular. However, the Noticee has attempted to take the easy way out by claiming that since it had surplus funds available, even if its own funds and client funds were mixed, it does not amount to violation of SEBI 1993 Circular. The mandate under the SEBI 1993 Circular is segregation of client and own funds, and not whether the Noticee had enough of its own funds deployed in the common pool account to use for its own purposes.

20. The Noticee has submitted on page 53 of its reply that the purpose and flow of funds from Citi Bank Pool Account, Axis Bank Pool Account, ICICI Bank Pool Account and HDFC Bank Pool Account is depicted in tabular form in annexure 8 of its reply (*i.e,* page 164 and 165 of annexure to reply). However, the said annexure does not contain any table. The said annexure states that there are four separate types of accounts maintained by the Noticee, which I have tabulated below for easy reference:

#	Purpose	Concerned bank account
1.	Account maintained for receiving funds from clients.	Details of relevant bank accounts not provided.
2.	Accounts maintained for pooling client funds and for meeting settlement obligation.	Citibank account bearing no. 340369335, IndusInd Bank account bearing no. 201000806715 and ICICI Bank account bearing no. 405100917
3.	Account maintained for payment of expenses, salary, vendor *etc.*	Details of relevant bank accounts not provided.
4.	Account maintained for meeting shortfall in pay-in obligation.	Citi Bank Pool Account, ICICI Bank Pool Account and ICICI Bank account bearing no. 405074198 *etc*

21. I find that although the Noticee in its reply has claimed that it maintains a separate account for receiving client funds, for pooling client funds, for meeting shortfall in pay-in and for payment of expenses, salary, vendor *etc*, it is contrary to the finding of the Comprehensive Inspection that Citi Bank Pool Account, Axis Bank Pool Account, ICICI Bank Pool Account and HDFC Bank Pool Account were being used for Noticee's own purposes as well. The Noticee has not furnished any explanation or evidence refuting the said finding, rather it has only claimed that it maintains separate accounts, which is grossly insufficient to discharge such a serious allegation. For example, annexure 6 of the SCN records sample entries which show that Citi Bank Pool Account was used by the Noticee for transferring money to and from IIFL Commodities. On March 24, 2014, the bank entry reads as "FOR ICD BEING AMT PAID TO IIFL COMMODITIES" and the amount debited is Rs. 100,000,000. The Noticee has not explained why such transaction was undertaken from an account which is maintained for meeting shortfall in pay-in obligation of clients. Thus, I am wholly unconvinced by the submission of the Noticee that it was maintaining separate accounts for its clients and for its own purposes.

22. The Noticee has contended that the entire broking industry was following the same practice of using a consolidated pool account for pay-in and pay-out of client funds and that any deficit in the pool account in meeting the stock exchange obligations would be met by IIFL through transfer of his own funds. I find that clause 1(B) of SEBI 1993 Circular allows stock brokers to maintain

a consolidated client account, however, by no means it permits the stock brokers to use the aforesaid pool account for its own purposes.

23. I find that the aforesaid acts of Noticee are in clear violation of clause 1(C) and clause 1(D) SEBI 1993 Circular which states that only the following money can be paid into and withdrawn from “clients account”:

<u>Money that can be paid into client account:</u>

(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 in the said circular;
(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.

<u>Money that can be withdrawn from client account:</u>

(i) money properly required for payment to or on behalf of clients; or
(ii) for or towards payment of a debt due to the member from clients; or
(iii) money drawn on client’s authority; or
(iv) money in respect of which there is a liability of clients to the member. However, the above withdrawal of moneys from clients’ account should not, in any case, exceed the total of the money so held for the time being for such each client.

24. With respect to the aforesaid allegation, the Noticee has also made detailed submission regarding the changes brought by it in its processes from October, 2014 onwards regarding its pool accounts. In this regard, since the inspection period for Adjudication Proceedings 1 is restricted to June, 2014, I do not find it necessary to analyze the changes so brought.

25. In light of the above discussion, I find that by mixing its own funds with client funds and using the aforesaid pool accounts for its own purposes, the Noticee has violated clause 1(C) and clause 1(D) of the SEBI 1993 Circular.

Allegations levelled in Supplementary Inspection I

26. I note that during Supplementary Inspection I, the following information was requested from the Company for sample 10 days:

(i) Aggregate value of debit balances of all clients as per trial balance across stock exchange (after adjusting for open bills of clients, uncleared cheques deposited by clients and uncleared cheques issued to clients).

(ii) Aggregate value of credit balances of all clients as per trial balance across stock exchange (after adjusting for open bills of clients, uncleared cheques deposited by clients and uncleared cheques issued to clients).

(iii) Total fund balance available in all client bank accounts maintained by the Company.

(iv) Aggregate value of collateral deposited with clearing corporations in form of cash and cash equivalents (fixed deposits, bank guarantees *etc*.)

27. I note that the said inspection records that on analysis of the aforesaid data submitted by the Company, it was observed that column F (total end of day balance in all client accounts available with the stock broker and collateral deposited with the clearing corporation/clearing member) was less than column B (aggregate client credit balance as per ledger). Since the aforesaid calculation resulted in a negative value, it was concluded that the said value indicates the extent of misutilization of client funds. The inspection also records that out of the selected 10 days, the credit client funds were

misutilized by the Company for settlement obligation of debit balance clients for 7 days.

28. The Noticee has contended that the practices followed by the Noticee were in line with the practices followed by the rest of the broking industry. All stock brokers, including IIFL, continued to receive funds from debtors/stock exchange and pay to creditors/ exchange on a continuous basis. The clients would pay-in by T+2+5 days whereas the brokers are required to pay by T+2 days to the stock exchanges, therefore, since most of the client funds are received from T+2 day onwards, the Noticee was applying its own funds to cover the shortfall. I find that the aforesaid contention of the Noticee amounts to admission that it was not segregating its own funds from client funds for the sake of running an efficient business and timely pay-in of client obligation. I find that if stock brokers are given liberty to deal and withdraw from the client account as and when they please, it would set a bad precedent as only in cases where an inspection has been carried out SEBI would discover that the stock broker has withdrawn in excess.

29. The Noticee has contended that even though the inspection period pertains to the period April 01, 2011 to June 30, 2014, SEBI has attempted to retrospectively apply the provisions of the Enhanced Supervision Circular which came into effect from July 01, 2017. It has further submitted that the following two considerations emerged out of the aforesaid circular which have been applied retrospectively in the present case:

(a) Considering 50% of the value of bank guarantees towards fund balances (*i.e.* only the funded portion) instead of the entire value of bank guarantee as stock exchanges have recourse to the full amount of bank guarantee upon invocation in case of any contingency; and

(b) Comparing ledger gross credit balances in client accounts with the client bank accounts and stock exchange accounts instead of comparing the ledger net credit balance (*i.e,* total creditors – total debtors) with the client bank accounts and stock exchange accounts which was the industry wide practice.

The Noticee has also furnished a recomputed working of the 10 days of the Supplementary Inspection I wherein it has been alleged that Company had misused the credit balance of its client funds for pay out obligations of its debit balance clients for 7 days after taking into account 100% of bank guarantee and net creditors balance. The revised working provided by the Noticee shows that the Noticee had excess cash available over net creditors on all 10 days.

30. I find that one of the major arguments of the Noticee in its reply is that there has been retrospective application of the Enhanced Supervision Circular in the present case as the SEBI 1993 Circular provides the purposes for which money can be drawn from the client accounts but does not specify the manner of calculation or adjustment or methodology for arriving at client balances. I have perused the judgments of the Hon'ble Supreme Court cited by the Noticee in support of the aforesaid contention, namely, *Binani Industries (supra) and Alliance* Finstock *Ltd. (supra)*. In my opinion, it cannot be said that the principles contained in the aforesaid circular are new principles altogether. The underlying principle against misutilization of client funds was already incorporated in clause 1(D) of the SEBI 1993 Circular. The principles based on which the misutilization calculation has been arrived at in the present case have always been a part of the working during inspections of stock brokers relating to segregation of funds and securities under the SEBI 1993 Circular. The Enhanced Supervision Circular codifies and streamlines the principles already enumerated in the SEBI 1993 Circular. Here, I find it appropriate to rely on the following orders passed by Hon'ble SAT wherein it has dismissed the aforesaid contention:

(i) <u>Kantilal Chhaganlal Securities Pvt. Ltd. vs. SEBI (Appeal No. 391 of 2020) decision dated March 24, 2022</u>: In this order, the inspection period was from April 01, 2014 to December 2015. Similar to the facts of the present case, the adjudicating officer had found that the appellant had violated the provisions of SEBI 1993 Circular by misutilizing client funds for other purposes. During the appeal before Hon'ble SAT, it was argued by the appellant that the Enhanced Supervision Circular was applied retrospectively in the case for imposing penalty. The Hon'ble SAT held the following:

"Having heard the learned counsel for the parties, we find that the contention raised by the appellant is patently erroneous. In this regard paragraph 1.D of the 1993 Circular states as under:-….

The aforesaid indicates that the broker shall not use funds of clients for any purpose other than client's own use…..

The aforesaid contemplates imposition of penalty in case of failure to segregate their own funds from that of the clients fund.

We find that the AO has dealt with the objection raised by the appellant and has held that the appellant has violated the 1993 Circular read with Regulation (26)(xiii) of the Brokers Regulations, 1992. In our opinion, the findings given by the AO in this regard does not suffer from any error of law." (emphasis supplied).

(ii) Arihant Capital Markets Ltd. vs. SEBI (Appeal No. 521 of 2019) decision dated October 21, 2021: In this appeal, the period of inspection was from April 01, 2014 to March 11, 2016. The Hon'ble SAT held as follows:

"The learned counsel for the appellant submitted before us that in the show cause notice the respondent had relied on a formula which, in fact, was not in existence at the time of the disputed period but was incorporated in circular dated September 26, 2016 which is brought into effect from July 1, 2017. He submitted that the formula would show that so far as the bank guarantee is concerned, only 50% of the same is

required to be considered and not 100% which has been considered in the cases of Axis Bank as detailed (supra).

Upon hearing both sides and upon perusing the relevant circulars, in our view, the order cannot be faulted with. The earlier circular had clearly stated that the funds of the client cannot be applied for any other purposes. The appellant's case was that the funds were applied by it for the dues for their associates, group company, etc. Now, during the arguments only, the issue of nonexistence of formula in the previous circular is brought up. In fact, the said formulization is nothing but the crystallization of the earlier circular.

In the circumstances, there is no merit in the appeal. The appeal is, therefore, dismissed without any order as to costs." (emphasis supplied)

In light of the above, I find that the contention of the Noticee that there has been retrospective application of Enhanced Supervision Circular in the present matter lacks merit.

31. The Noticee has contended that the entire portion of the bank guarantee should be considered as opposed to only 50% considered by the inspection team. I find that the value of bank guarantee is considered to be 50% (half) since the funds deposited with the bank for availing the bank guarantee is only 50%. Basis 50% of the funds deposited by the stock broker with the bank, the bank provides 100% bank guarantee. I note that during the inspections the Noticee has acknowledged that bank guarantees are issued to it with 50% cash margin under lien to the bank and supporting evidence in this regard has also been provided. Thus, I cannot accept the argument of the Noticee that 100% of the bank guarantee should be considered. Further, Noticee's contention that the concept of considering 50% bank guarantee is arising out of Enhanced Supervision Circular, and therefore, it should not be applied to the facts of the present case is not logical as it is a matter of fact that the Noticee has deposited 50% as collateral for obtaining 100% bank

guarantee. I am unable to understand how 100% of bank guarantee can be considered under total funds available with the stock broker, when in fact, it is has not given the entire 100% as collateral.

32. The Noticee has also contended that net creditors balance (*i.e,* total creditors-total debtors) should be considered instead of aggregate credit client balance while calculating the value of “G”. I find that if the aforesaid interpretation is adopted, then it would mean that a broker paying from the excess funds of one client to meet the liability of another client is acceptable, which is completely contrary to the requirements of the SEBI 1993 Circular which envisages maintenance of credit balance funds at all times. I find that a similar contention was raised before the Hon’ble SAT in the matter of ***Sushil Financial Services Pvt. Ltd. vs. SEBI***, (Appeal No. 196 of 2016), decision dated November 06, 2019, wherein it held that:

“As regards the second charge, the appellant explained that only some of credit balances of all credit clients should not be considered for verifying funds lying in the bank accounts as the same would be in isolation, because pay-in and pay-out happens on net basis and hence even debit balances of all debit clients should be considered. Emphasizing on the net basis pay-in and pay-out, the appellant contended that settlement at member level shall not be considered and thus, the allegation that the credit funds of the clients was used is wrong. The AO however observed that the submission cannot be accepted as the funds of credit balance client was used for obligation of debiting balance client. Further, it was pointed that the account of the credit balances clients account had eroded by adopting the said practice. It was found that the said practice was in violation of SEBI circulars dated November 18, 1993 and August 27, 2003.

In our view, while the violation as regard the first charge is admitted by the appellant, the explanation regarding the second charge is not acceptable. The clients account cannot be tinkered with that for pay-in and pay-out on net basis of the appellant.

In the present case, what we find is that the appellant has accepted the cash transactions from SGCPL and vice versa. <u>As regards the second charge, the same is also established</u>, in view of the admission by the appellant by terming it as practice" (emphasis supplied)

33. The argument of the Noticee that value at risk (VaR) and exposure margin has not been considered during inspection is incorrect. The VaR margin and exposure margin has been deposited by the Noticee with the stock exchanges, thus, the funds portion of the margin paid by the Noticee has already been taken into consideration in the calculation of collateral available with the stock exchanges. Margin paid to the stock exchanges in the form of securities cannot be considered for the purpose of assessing misuse of client funds. In light of the above, if the VaR margin and exposure margin is considered again it would amount to double counting. Thus, this argument of the Noticee is not acceptable. As regards the submission of the Noticee that the aggregate value of collaterals deposited with clearing corporation does not take into account the deposits made with the exchanges towards disputed clients, arbitration claims *etc,* I find that the Noticee has failed to provide any documentary evidence to substantiate that if the aforesaid additional items were to be taken into account the charge of misutilization of client funds would not sustain.

34. In context of the aforesaid paragraphs, I do not find any difficulty in dismissing the revised calculation for 10 days furnished by the Noticee and holding that the Noticee has contravened the provisions of SEBI 1993 Circular.

<u>Allegations levelled in Supplementary Inspection II and Supplementary Inspection III</u>

35. I note that the Noticee has submitted a revised table with respect to the allegations levelled in Supplementary Inspection II that out of the 105 days examined, the Noticee has (i) used funds of the credit balance clients for its

debit balance clients for 101 days; and (ii) out of the said 101 days, used funds of credit balance clients for proprietary trading for 13 days. Further, the Noticee has also furnished a revised table with respect to the allegations levelled in Supplementary Inspection III that out of the 695 days examined, the Noticee has: (i) used funds of credit balance clients for its debit balance clients for 687 days; and (ii) out of the said 687 days, used credit client funds for settlement obligation of debit balance clients and proprietary purposes for 29 days.

36. I find that the revised tables provided are based on the same considerations which the Noticee has used for its revised calculation of 10 days under Supplementary Inspection I, which are (i) considering 100% bank guarantee instead of 50% bank guarantee; and (ii) considering net creditors instead of ledger credit balance of its clients. It is pertinent to highlight here that *vide* letter dated January 20, 2016, the Noticee has admitted the charge levelled against it that it had used credit balance client funds for debit balance client funds, the relevant extract of the Noticee's admission is reproduced below:

"d) Accordingly, we submit that utilization of client funds towards clients debit balance are in compliance with set systems and process by the Exchanges. The same is followed in the industry"

37. Since I have already dealt in the previous paragraphs as to why 100% bank guarantee, net creditors, VaR, exposure margin, deposits with stock exchanges for disputed clients, arbitration claims *etc* should not be considered for calculating misutilization of client funds by the Noticee in the present case, the same reasoning in is applicable in full force to the contentions of the Noticee with respect to findings of Supplementary Inspection II and Supplementary Inspection III. The explanation provided therein is not reproduced here for the sake of brevity. Thus, I find that the Noticee has violated the provisions of the SEBI 1993 Circular by:

(i) utilizing funds of credit balance clients for settlement obligation of debit balance clients for 101 days from the sample selected in

Supplementary Inspection II and thereby misutilized client funds ranging from Rs 1.09 crores to Rs 397.02 crores;

(ii) utilizing funds of credit balance clients for settlement obligation of proprietary trades for 13 days out of the 101 days in Supplementary Inspection II and thereby misutilized client funds ranging from Rs. 2.02 crores to Rs.73.28 crores;

(iii) utilizing funds of credit balance clients for settlement obligation of debit balance clients for 687 days out of sample selected in Supplementary Inspection III and thereby misutilized client funds ranging from Rs. 0.58 crores to Rs. 309.23 crores;

(iv) utilizing funds of credit balance clients for settlement obligation of debit balance clients and proprietary trades for 29 days out of 687 days in Supplementary Inspection III and thereby misutilized client funds ranging from Rs. 0.26 crores to Rs. 42.51 crores.

38. The Noticee has argued that during the years 2011-2014, the Noticee had net worth of over Rs 1200 crores, out of which it had approximately Rs. 400 crores to Rs. 600 crores available for meeting any shortfall in client pool account. However, I find that the net worth analysis done by the inspection team after scrutinizing the balance sheet as on March 31, 2012, paints a different picture. Paragraph 11 of the SCN states that as on March 31, 2012, the Noticee had only Rs 69.05 crores of net worth available for running the broking activities. It further states that out of the aforesaid amount, Rs 56.95 crores were invested in fixed assets, deferred tax assets, short term loans & advances and current investment, which leaves the Noticee with Rs 12.1 crores. Rs 12.1 crores was further invested by the Noticee in long-term loans & advances, other current assets and inventories. *Firstly*, I find that the Noticee has unsuccessfully tried to shield itself from the charge of violation of SEBI 1993 Circular by citing that it had sufficient net worth. I find that the question of net worth becomes relevant only when the Noticee defaults in its obligation whereas in the present matter the charge alleged against the

Noticee is misutilization of client funds. Merely because the Noticee claims that it had sufficient net worth, does not permit the Noticee to flout the provisions of SEBI 1993 Circular. *Secondly*, even if net worth were to be taken into account, I find that as evidence the Noticee has furnished a copy of net worth certificate given by its chartered accountants (annexure 10 of its reply) which states that as on March 31, 2013, the Noticee's net worth was Rs 13,100,298,395. I find that the aforesaid certificate does not give insight into the net worth available for deployment. Thus, I am completely unsatisfied with respect to the net worth argument advanced by the Noticee.

<u>Other contentions of the Noticee</u>

39. The Noticee has also submitted that findings of NSE and BSE arising out of the joint inspection undertaken by SEBI, NSE and BSE, did not record any adverse observations regarding segregation of client funds and third party funding/transaction. It has further submitted that SEBI has not taken into account findings, action taken reports, penalties and conclusion of actions of NSE and BSE. Herein, the joint inspection being referred to by the Noticee is the Comprehensive Inspection. In this regard, it is pertinent to note that since the Comprehensive Inspection was done on sampling basis, the instances of irregularities and violations pointed out in the inspection report are not exhaustive in nature. It is also important to note that the scope of inspection and methodology of SEBI while conducting inspection would not be completely parallel to the ones adopted by NSE and BSE. Thus, *prima facie*, the findings of SEBI and the stock exchanges can be distinguished on the aforesaid grounds alone. Assuming whilst denying that there is any merit in the submission of the Noticee that paragraph 1.14 of the inspection report sent to it by NSE does not record any adverse findings with respect to segregation of funds by Noticee, I note that the said paragraph under the head "sampling" *inter alia* states that:

"2 Dates-BSE, 2 Dates-NSE top 100 transactions from each dates for pay in/pay out of securities

Scrutiny of all the bank books of IIFL, of 1 month".

From the aforesaid, I find that it is clear that the sample size used by NSE and BSE for assessing pay in and pay out of funds and securities of clients was only 2 dates, which by itself is an unarguably small sample size. Further, I find that the aforesaid sample was further refined by top 100 transactions of each day. As opposed to the sample size of NSE and BSE, SEBI has analyzed multiple pool accounts of the Noticee during Comprehensive Inspection, 20 days during Supplementary Inspection I, 105 days during Supplementary Inspection II and 695 days during Supplementary Inspection III. Thus, I find that depending on the sample size and the particular dates selected for sampling, the findings can differ, which is what has happened in the present case. Therefore, the aforesaid contention of the Noticee is trifle and feeble.

40. The Noticee has argued that since it has not misutilized client funds, the question of ill-gotten gains does not arise. I completely disagree with the aforesaid contention in light of my observations recorded in paragraphs above. It is noted from the inspections undertaken that the Noticee has misused client funds in the range of Rs 0.59 cores to Rs 397.02 crores for settlement obligation of debit balance clients and in the range of Rs 0.26 crores to Rs. 73.28 crores for proprietary purposes, in addition to settlement obligation of debit balance clients. The misutilisation amount of each day was multiplied with the rate of borrowing and it was concluded that the interest on funds misused by the Noticee amounted to Rs. 34.87 crores. I note that the detailed statement showing the interest on funds misused was provided as annexure 18 of SCN.

41. The Noticee has raised suspicion over the method of calculation of the amount of ill-gotten gains. It has contended that the amount of Rs. 34.87 crores arrived at by SEBI is a notional figure after considering hypothetical interest rates assuming that borrowing would be required to fund debit

balances. I note that the SCN in paragraph 12 records that the aforesaid interest amount was arrived at in the following manner:

(i) Since IIFL did not have outstanding borrowings during certain financial years to enable calculations, the average borrowing rate was calculated by dividing interest cost by average indebtedness based on the consolidated financial statements of its holding company *i.e.,* IIFL Holdings Ltd (IIHL).

(ii) Further, the daily balance amount misused by the Company for settlement obligation of debit balance clients/proprietary purposes was multiplied with the daily borrowing cost of IIFL Holdings Ltd (IIHL).

42. I find that it has been explicitly recorded in the SCN that the reason for calculating the rate of interest from the financial statements of its holding company is that the Noticee did not have any outstanding borrowings during certain financial years. Both IIFL Holdings Ltd (IIHL) and the Noticee are in the business of providing financial services. Given that the nature of business of IIHL (holding company) and the Noticee was similar, and in absence of a better reference rate, I find that it is logical to use the rate of borrowing of the holding company for the subsidiary company as it is highly probable that the subsidiary company would borrow at a similar rate of interest as its holding company. I also note that the Noticee has merely claimed that the interest rate is hypothetical without furnishing an alternate interest rate which would be better suited to derive the cost of borrowing of the Company and the calculations resulting from it. The Noticee has also argued that it has been assumed that the Noticee would necessarily need to borrow to fund its debit balance clients. Since it has been established above that Noticee had misused funds of its credit balance clients, it is a plausible conclusion that the Noticee did not have sufficient funds/did not intend to use funds available for funding its debit balance clients or for carrying out its proprietary trades. Thus, I find no difficulty in holding that the interest on funds misused by the Company was Rs. 34.87 crores.

43. With respect to the cases cited by the Noticee in paragraph 9.12 above, wherein it has been held that non segregation of client funds and/or misutilization of client funds amount to technical lapses and for which a letter of warning was issued as punishment, my findings are provided below:

(i) I find that order passed by the Whole Time Member in the matter of M/s. J. M. Morgan Stanley Retail Services Pvt. Ltd. dated June 02, 2004, does not apply to the facts of the case at all. An extract from the said order is reproduced below which will make my finding crystal clear:

"I agree with the Enquiry Officer's finding that the charge regarding the member having failed to maintain separate client account in respect of some clients cannot be sustained…."

In the present case, based on my reasoning above, I have found that the Noticee is in violation of the SEBI 1993 Circular, however, in the aforesaid case, no violation with respect to segregation of client funds was found, so naturally, if letter of warning was issued in the said case or not becomes inconsequential to the case at hand.

(ii) With respect to the order passed by Chairman in the matter of M/s. Bama Securities Ltd. dated June 04, 2004, I find that the said case did not contain the allegation that the broker had failed to segregate client funds or had mistutilized client funds, thus, the fact that letter of warning was issued in the aforesaid matter has no bearing in the present case as the allegations itself are different.

(iii) In the order passed by Whole Time Member in the matter of M/s. Bakliwal Investment, dated May 18, 2004, I note that the inspection period was from the year 1999 to 2000. Further, with respect to similar allegations, the Whole Time Member had *inter alia* recorded the following:

“4.1.4 The broker mis-used client account by adjusting one account with another without proper authorization. The broker had submitted that the authorizations / consent letters were filed but were not produced. The broker further submitted that all the clients whose accounts were adjusted with another were sister concerns. The submission of the broker on this issue is not satisfactory. The broker should not have misused client account by adjusting one account with another without proper authorization irrespective of the number of cases where it was done or the fact that all the clients were sister concerns.

4.1.6 Broker had used clients’ bank account accounts for the purpose other than what is stipulated. The broker had submitted that Global Trust Bank had directly debited demat charges and bank guarantee commission to its account without an instruction from the broker. The broker further submitted that Global Trust Bank was instructed not to carry on such debits. However, the broker failed to produce any document to show such debits were credited back. I find that there were only 11 transactions of small amount and in only one bank i.e., Global Trust Bank.”

I find that the aforesaid case can be distinguished on three grounds. *Firstly*, the inspection period in the present case is longer than the inspection period of the aforesaid case, which in light of my findings above shows that the violation committed by the Noticee is more repetitive than the violation in the aforesaid case. *Secondly*, with respect to misusing client funds, in the aforesaid case there has been no finding regarding the range of misutilization, whereas in the present case, the range of misutilization is between Rs 0.59 crores to Rs 397.02 crores, therefore as is not on record what the misutilization amount was in the aforesaid case, I find that it cannot be compared with the present case. *Thirdly*, with respect to using clients bank account for other purposes, I find that it has been recorded in the aforesaid case that the concerned transactions were of miniscule amount, however, the same cannot be said in the present case in light of the misutilization range cited above.

(iv) As regards the order passed by Whole Time Member in the matter of Twenty First Century Shares and Securities Limited, dated December 30, 2005, I find that the following extract from the aforesaid order needs to be highlighted:

"iv. With regard to non segregation of client and own funds, the inspection report cites 25 instances where transactions not pertaining to the clients were routed through the client's bank account. After considering the reply of the broker that out of the 25 instances, 17 are for the re-payment of EMI for the car belonging to the broker's holding company, non involvement of any outside clients, <u>absence of any allegation in the inspection report regarding mis-utilisation of the client's money, and taking into account the rectification of the deficiencies has suggested that the broker may be warned for the irregular practice."</u> (emphasis supplied)

I find that since the allegation of misutilization was not dealt in the aforesaid order, the Noticee cannot seek parity by placing reliance on it.

(v) I find that contrary to the Noticee's claim that non segregation and misuse of client funds was held as a technical lapse pursuant to which a letter of warning was issued in the order passed by Whole Time Member in the matter of Mahesh Kothari Share and Stock Brokers Pvt. Ltd., dated October 08, 2012, I find that in the said order the Whole Time Member had suspended the certificate of registration of the broker for 2 months. Thus, the Noticee's reliance on the aforesaid case for supporting its contention is misplaced.

(vi) The Noticee has also placed reliance on the order passed by the Hon'ble SAT in the matter of Chona Financial Services Pvt. Limited dated August 23, 2004, wherein the Hon'ble SAT had modified the penalty to a warning with respect to an appellant who was *inter alia* charged with the allegation of non-segregation of client's fund and misutilization of client account. I note that the aforesaid case was distinguished by Hon'ble SAT itself in ***K. Seetharam vs. SEBI*** (Appeal No: 86 of 2005) decision dated July 07, 2005, wherein it held that:

"The appellant has requested to cancel the penalty considering the facts and circumstances of the case. He has further stated in the appeal that where similar violations along with other violations had occurred, this Tribunal has reduced the penalty to a mere warning. He has cited the following judgments of the Tribunal:

i. Intech Shares and Stock Brokers Vs. SEBI
ii. Sumedha Fiscal Services Ltd. Vs. SEBI
iii. Prakash K. Shah Shares and Securities Pvt. Ltd. Vs. SEBI
iv. Bakliwala Investment
v. J.M. Morgan Stanley Retail Services Pvt. Ltd.
vi. Bama Securities
vii. Shyama Sundar Dalmia Vs. SEBI
viii. Sanjay C. Bakshi
ix. Mahesh Kothari Shares and Stock Brokers Pvt. Ltd.
x. Kumesh Sawney
xi. <u>Chona Financial Services Pvt. Ltd.</u>

10. <u>We have gone through the documents submitted by the appellant and the facts of the case. We have also gone through some of the judgments cited in the appeal. While it is a fact that in all these cases the Tribunal has modified the order of the respondent but we must admit that each case is a different case and decision is taken on the facts and circumstances of each case.</u> Each order sets out detailed finding and reasons for taking action or imposing the penalty. In this *particular case we have to examine basically two issues. (emphasis supplied)*

44. The Noticee has contended that the alleged findings under the SCN does not make a reference to any specific provision of the SEBI 1993 Circular, which shows that the inspection team has not understood the facts of the case and the specific provisions of the SEBI 1993 Circular. I find that not specifying the exact provisions of the SEBI 1993 Circular alleged to have been violated by the Noticee does not reflect on the competency of the inspection team regarding understanding the facts of the current case and/or the provisions of SEBI 1993 Circular. I find that such a bald statement is unwarranted. I find that the acts of the Noticee established in the preceding paragraphs clearly fall foul of clauses 1(B), 1(C) and 1(D) of the SEBI 1993 Circular. On a joint reading of the allegations levelled in the SCN and the aforesaid clauses, it becomes sufficiently clear that the Noticee has violated clauses 1(B), 1(C) and 1(D) of the SEBI 1993 Circular. Thus, I find that this submission of the Noticee does not have any bearing on the outcome of the present proceedings.

45. The Noticee has provided a tabular analysis with respect to compliance of the Noticee with each of the clauses of SEBI 1993 Circular (annexure 4 of its reply). I find that merely putting no adverse findings were alleged in the SCN for each of the clauses of SEBI 1993 Circular does not help the case of the Noticee. Analysis of Citi Bank Pool Account, Axis Bank Pool Account, ICICI Bank Pool Account and HDFC Bank Pool Account during the Comprehensive Inspection had clearly revealed that the Noticee was using the aforesaid pool accounts for its own purposes which the Noticee has not been able to rebut in its reply. Further, as recorded above, the Noticee has also not been able to explain the reasoning for negative value of “G” column observed in the supplementary inspections. Thus, I find that submitting such a hollow analysis of compliance with the provisions of SEBI 1993 Circular is a futile attempt which does not deserve any further deliberation.

46. The Noticee has submitted that it has fully implemented the system prescribed under the Enhanced Supervision Circular and it has also furnished copies of compliances and reporting of balances for July, 2017. Further, the Noticee has relied upon the decisions of Hon'ble SAT in M/s. DSE Financial Services Ltd. (Appeal no. 153 of 2012), dated September 11, 2012 and UPSE Securities Limited vs. SEBI (Appeal no. 109 of 2011), dated July 25, 2011 to submit that in view of prompt rectification/ implementation by the broker, the proceedings should be dropped. I have perused the aforesaid orders. *Firstly*, I find that the aforesaid orders are distinguishable on facts. In *DSE Financial Services Ltd. (supra),* the violation committed by the broker was failure to maintain records in the manner specified, and in *UPSE Securities Limited (supra),* the violation committed by the broker was (i) allotting of more than one terminal to the same user at different addresses; and (ii) not allotting unique client code to clients, the aforesaid violations are nowhere related to the violations involved in the present matter. *Secondly*, even if the principle laid down by Hon'ble SAT in the aforesaid matters is to be considered that every minor irregularity/technical violation does not warrant punitive action, I find that by no stretch of imagination misutilization ranging upto Rs 397.02 crores can be considered as minor irregularity or technical violation on the part of the Noticee.

47. The Noticee has also relied upon 13 adjudication orders to contend that in similar facts and allegations minimal penalties have been imposed. I have perused the contents of the aforesaid orders as well as the penalties levied therein. I find that the present case is a unique case where over the course of 3 years and 5 separate inspections, violation of provisions of SEBI 1993 have been observed against the Noticee. Apart from not designating client bank accounts as “client account”, I find that the other violations observed against the Noticee are grievous in nature. This is not a case where the contravention is on account of any doubt or disability of the Noticee to perform its duties. By deliberately misusing client funds, the Noticee has taken undue advantage of the trust of lakhs of investors who have deposited their hard earned money in the hands of the Noticee. I find that given the

frequency and the gravity of violations, the Noticee has laid the investors as well as the integrity of the securities market on the line, and therefore, it does not deserve any leniency.

II. Issue No. II: If yes, whether the violation, on the part of the Noticee would attract monetary penalty under section 23D of SCRA?

III. Issue No. III: If the answer to Issue No. II is in affirmative, what would be the monetary penalty that can be imposed upon the Noticee taking into consideration the factors stipulated in section 23J of SCRA read with rule 5(2) of SCRA Adjudication Rules?

48. Since violation of provisions of SEBI 1993 Circular by the Noticee is established, I am of the view that the same warrants imposition of monetary penalty upon the Noticee under section 23D of SCRA, text of which is provided below:

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].*

*******Substituted for the words "liable to a penalty not exceeding one crore rupees" by the Securities Laws (Amendment) Act, 2014, w.e.f 08-09-2014.*

49. While determining the quantum of penalty under section 23D of SCRA Act, the following factors stipulated in section 23J of SCRA, have to be given due regard:

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

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

(c) the repetitive nature of the default.

50. The material made available on record has quantified the interest on funds misused by the Noticee at Rs 34.87 crores. The inspection has not quantified the loss caused to the investors. However, with respect to the repetitive nature of the default, as brought out before, the violations committed by the Noticee have been observed over multiple inspections, thus, it would be appropriate to consider them as repetitive.

E. ORDER

51. After taking into consideration all the facts of the case and the contentions of the Noticee, in exercise of powers conferred upon me under section 23-I(2) of SCRA read with rule 5 of the SCRA Adjudication Rules, I hereby impose a penalty of Rs. 1,00,00,000/- (Rupees One Crore Only) upon the Noticee *i.e.,* India Infoline Limited *(now known as IIFL Securities Ltd.)* under section 23D of SCRA for violation of the provisions of SEBI 1993 Circular.

52. The said penalty imposed on the Noticee, as mentioned above, is commensurate with the violation committed by the Noticee and acts as a deterrent factor for the Noticee and others in protecting the interest of investors.

53. The Noticee shall remit / pay the said amount of penalty within 45 days of receipt of this order either by way of demand draft in favor of "SEBI - Penalties Remittable to Government of India", payable at Mumbai, or through

online payment facility available on the SEBI website **www.sebi.gov.in** on the following path by clicking on the payment link.

ENFORCEMENT → ORDERS → ORDERS OF AO → PAY NOW

In case of any difficulties in payment of penalties, the Noticee may contact the support at portalhelp@sebi.gov.in.

54. The Noticee shall forward the said demand draft or the details / confirmation of penalty so paid through e-payment to the Division Chief, Enforcement Department-I, DRA-III, SEBI, in the format given in table below:

1.	Case name	
2.	Name of payee	
3.	Date of payment	
4.	Amount paid	
5.	Transaction no	
6.	Bank details in which payment is made	
7.	Payment is made for	Penalty

55. In terms of rule 6 of the SCRA Adjudication Rules, copies of this order are sent to the Noticee and SEBI.

Date: May 20, 2022
Place: Mumbai

PRASANTA MAHAPATRA
ADJUDICATING OFFICER