BEFORE THE ADJUDICATING OFFICER

SECURITIES AND EXCHANGE BOARD OF INDIA

(ADJUDICATION ORDER NO: Order/AS/VC/2024-25/31028-31031)

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

In respect of

Noticee No.	Name and PAN of the Noticee
1	Rikhav Securities Limited (PAN- AADCR3067Q)
2	Hitesh Himatlal Lakhani (PAN- AAAPL3243L)
3	Monil Rajendra Shah (PAN- CMFPS8839A)
4	Dharmesh Navalchand Shah (PAN- AADPS3565M)

In the matter of Rikhav Securities Limited

BACKGROUND OF THE CASE

1. Securities and Exchange Board of India (hereinafter referred to as **"SEBI"**) had carried out a comprehensive joint inspection (along with Exchanges) of Rikhav Securities Ltd (hereinafter referred to as **"Noticee-1/ Rikhav"**) during October 12, 2022 to October 21, 2022. The period of inspection was from April 01, 2021 to September 30, 2022 (hereinafter referred to as the **"IP"**).

2. Based on the findings of inspection in the matter, SEBI initiated adjudication proceedings against Rikhav Securities Limited, and its directors Hitesh Himatlal Lakhani **("Noticee-2")**, Monil Rajendra Shah **("Noticee-3")** and Dharmesh Navalchand Shah (**"Noticee-4"**) [hereinafter collectively referred to as "**Noticees"**] under Section 15-I of the SEBI Act, 1992 for alleged violation of the following provisions of Rules, SEBI Regulations and Circulars:

Table No. 1

Sr. No.	Alleged violations pertaining to	Regulatory provisions violated
(i)	Stock reconciliation	Clause 2.3 of SEBI Circular MRD/DoP/SE/Cir-11/2008 dated April 17, 2008.
(ii)	Stock mismatch alerts	Clauses 6.1.1(j) & 7.1.2 of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016.
(iii)	Monthly/Quarterly settlement of funds	Clause 12(e) of Annexure-A of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009 read with Clause 8.1 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016 and Clause no. 5.4. of SEBI circular SEBI/HO/MIRSD/DOP/P/CIR/2021/577 dated June 16, 2021.
(iv)	Reporting and short collection of Margin	SEBI Circular No. CIR/DNPD/7/2011 dated August 10, 2011 read with Clause (iii) of Annexure to SEBI Circular No. SEBI/HO/MRD2/DCAP/CIR/P/2020/127 dated July 20, 2020.
(v)	Client registration process	SEBI Circular CIR/MIRSD/16/2011 dated August 22, 2011 and SEBI circular CIR/HO/MIRSD/DOP/CIR/P/2019/75 dated June 20, 2019; Clause 13(b) and 13(c) of Annexure 6 of SEBI Circular CIR/MIRSD/16/2011 dated August 22, 2011 read with SEBI circular CIR/HO/MIRSD/DOP/CIR/P/2019/75 dated June 20, 2019; BSE Circular Notice No. 20210727-6 dated July 27, 2021 read with Clause A(5) in

Sr. No.	Alleged violations pertaining to	Regulatory provisions violated
		Schedule II (Code of Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992.
(vi)	Net worth verification	Clause 6.1.1(j) of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016.
(vii)	Verification of weekly holding statement	Clause 3 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016.
(viii)	Verification of Unique Client Code (**"UCC"**)	Clause 2(B) of SEBI Circular CIR/MIRSD/15/2011 dated August 02, 2011.
(ix)	Member engaged as a principal or employee in a business other than that of securities involving personal financial liability	Rule 8(3)(f) of Securities Contract (Regulation) Rules, 1957 ("SCR Rules"), NSE circular No. NSE/COMP/50957 dated January 07, 2022.
(x)	Trading in minor's accounts	SEBI FAQ on demat/trading account for minors dated September 25, 2018 read with Clause A(2) in Schedule II (Code of Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992.
(xi)	Dealing with unregistered constituents	Regulation 3.1.4 read with Regulation 3.1.8 of Part A of Capital market Regulation of NSE and Regulation 3.1.19 of Regulations (F&O segment) of NSE read with Clause A(5) in Schedule II (Code of Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992.
(xii)	Cyber security and cyber resilience	SEBI circular SEBI/HO/MIRSD/CIR/PB/2018/147 dated December 03, 2018 and

Sr. No.	Alleged violations pertaining to	Regulatory provisions violated
		SEBI/HO/MIRSD/TPD/P/CIR/2022/80 dated June 07, 2022.
(xiii)	Non co-operation with inspection team	Regulation 21 of Securities and Exchange Board of India (Stock Brokers) Regulations, 1992.

APPOINTMENT OF ADJUDICATING OFFICER

3. SEBI had appointed Shri Biju S. as the Adjudicating Officer ('AO') under Section 19 of SEBI Act, 1992 read with Section 15-I of SEBI Act, 1992 and Rule 3 of SEBI (Procedure for Holding Inquiry and Imposing Penalties), 1995 (hereinafter referred to as **"AO Rules"**) vide *communiqué* dated March 20, 2024 to adjudicate upon the alleged violations done by the Noticees. Subsequently, pursuant to transfer of erstwhile AO, undersigned was appointed as AO in the matter *vide* order dated July 22, 2024.

SHOW CAUSE NOTICE, REPLY AND HEARING

4. Show Cause Notice bearing reference no.- SEBI/EAD-1/BS/14848/1/2024 dated April 19, 2024 (hereinafter referred to as **"SCN"**) was issued to the Noticees in terms of the provisions of Rule 4(1) of the AO Rules read with Section 15-I of the SEBI Act, 1992, requiring the Noticees to show cause as to why an inquiry should not be held against it and why penalty, if any, should not be imposed upon the Noticees under Section 15HB of SEBI Act, 1992 for the alleged violations. I note that the SCN issued to Noticees was duly served upon the Noticees and it was acknowledged by the Noticees. *Vide* letter dated May 23, 2024, Noticees requested for inspection of the documents in the matter, which was granted to them on August 23, 2024. After inspection of documents on August 23, 2024, Noticees were advised to furnish reply to the SCN by September 13, 2024, *vide* e-mail dated August 29, 2024. Further, Noticees, *vide* letter dated September 06, 2024, requested for extension of time for filing their reply to the SCN, which was

granted to them. Thereafter, *vide* letter dated October 03, 2024, Noticees submitted their common reply to the SCN. Noticees also made common additional submissions in the matter *vide* e-mail/ letter dated October 14, 2024.

5. In the interest of natural justice, an opportunity of hearing on September 20, 2024 was granted to the Noticees *vide* Hearing Notice dated August 29, 2024. *Vide* letter dated September 06, 2024, Noticees sought adjournment of hearing and requested to re-schedule the hearing after October 05, 2024. Accordingly, hearing in the matter was re-scheduled on October 07, 2024. On October 07, 2024, Authorized Representatives (**"ARs"**) of the Noticees attended the hearing in person at SEBI and reiterated the submissions made by the Noticees *vide* letter dated October 03, 2024. Further, ARs stated to make the additional submissions in the matter, which were made by the Noticees *vide* letter dated October 14, 2024.

CONSIDERATION OF ISSUES AND FINDINGS

6. I have carefully perused the charges levelled against the Noticees in the SCN, submissions made by the Noticees and material available on record. The issues that arise for consideration in the present case are as follows:

   I. Violation of the provisions of the Rules, SEBI Regulations and Circulars:

   (a) Whether Noticee-1 has violated the provisions of the Rules, SEBI Regulations and Circulars as mentioned in para no. 2 hereinabove?

   (b) Whether Noticee- 2, 3 and 4 have violated the provisions of the Rules, SEBI Regulations and Circulars as mentioned in para no. 2 hereinabove?

   II. Does the violation, if any, attract monetary penalty under Section 15HB of SEBI Act, 1992?

   III. If so, what would be the monetary penalty that can be imposed upon the Noticees taking into consideration the factors stipulated in Section 15-J of the SEBI Act, 1992 read with Rule 5(2) of the AO Rules?

7. Before proceeding further, it is pertinent to refer to the relevant provisions of Rules, SEBI Regulations and Circulars which are alleged to have been violated. The said provisions are reproduced hereunder for ease of reference:

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

2. *In continuation of earlier circulars and in order to reiterate the need for brokers to maintain proper records of client collateral and to prevent misuse of client collateral, it is advised that:- The records should be periodically reconciled with the actual collateral deposited with the broker.*

SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016:

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

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

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

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

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

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

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

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

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

__P-__ Aggregate value of Proprietary Margin Obligation across Stock Exchanges

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

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

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

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

Principle:

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

$$G = (A+B)-C$$

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

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

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

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

$$H = |G| - |D|$$

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

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

Principle:

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

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

The sum of the proprietary funds (positive value of G), the value of proprietary securities (E) and the non-funded portion of bank guarantee (F) available in the Stock Exchanges is compared with the Proprietary margin obligations (P). If P > (G+E+F), then Stock Exchange shall calculate the difference I, which is the amount of proprietary margin obligation funded from clients assets.

$$I = P - (G+E+F)$$

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

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

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

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

Principle:

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

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

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

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

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

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

The value of J, if positive, indicates the extent of clients' funds utilised towards margin obligations of debit balance clients and proprietary margin obligations. This value of J acts as an alert to the Stock Exchanges on the possible mis-utilisation of clients' funds towards margin obligations of debit balance clients and proprietary margin obligations.

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

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

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

6.1.1. Monitoring criteria for Stock Brokers –

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

7. Uploading clients' fund balance and securities balance by the Stock Brokers on Stock Exchange system

7.1.2. End of day securities balances (as on last trading day of the month) consolidated ISIN wise (i.e., total number of ISINs and number of securities across all ISINs).

8. Running Account Settlement

8.1. In partial modification of circular on running account settlement, the stock broker shall ensure that;

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

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

8.1.3. The required bank details for initiating electronic fund transfers shall be obtained from new clients and shall be updated for existing clients. Only in cases where electronic payment instructions have failed or have been rejected by the bank, then the stock broker may issue a physical payment instrument.

8.1.4. Statement of accounts containing an extract from client ledger for funds & securities along with a statement explaining the retention of funds/securities shall be sent within five days from the date when the account is considered to be settled.

Clause 12(e) of Annexure-A of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009:

The actual settlement of funds and securities shall be done by the broker, at least once in a calendar quarter or month, depending on the preference of the client. While settling the account, the broker shall send to the client a 'statement of accounts' containing an extract from the client ledger for funds and an extract from the register of securities displaying all receipts/deliveries of funds/securities. The statement shall also explain the retention of funds/securities and the details of the pledge, if any.

Clause no. 5.4. of SEBI circular SEBI/HO/MIRSD/DOP/P/CIR/2021/577 dated June 16, 2021:

For the clients having credit balance, who have not done any transaction in the 30 calendar days since the last transaction, the credit balance shall be returned to the client by TM, within next three working days irrespective of the date when the running account was previously settled.

Clause (iii) of Annexure to SEBI Circular No. SEBI/HO/MRD2/DCAP/CIR/P/2020/127 dated July 20, 2020:

The member shall have to report the margin collected from each client, as at EOD and peak margin collected during the day, in the following manner:

a) EOD margin obligation of the client shall be compared with the respective client margin available with the TM/CM at EOD.

AND

b) Peak margin obligation of the client, across the snapshots, shall be compared with respective client peak margin available with the TM/CM during the day.

Higher of the shortfall in collection of the margin obligations at (a) and (b) above, shall be considered for levying of penalty as per the extant framework.

Clause 13(b) and 13(c) of Annexure 6 of SEBI Circular CIR/MIRSD/16/2011 dated August 22, 2011:

***13.** In case you have given specific authorization for maintaining running account, payout of funds or delivery of securities (as the case may be), may not be made to you within one* *working day from the receipt of payout from the Exchange. Thus, the stock broker shall maintain running account for you subject to the following conditions:*

(b) The actual settlement of funds and securities shall be done by the stock broker, at least once in a calendar quarter or month, depending on your preference. While settling the account, the stock broker shall send to you a 'statement of accounts' containing an extract from the client ledger for funds and an extract from the register of securities displaying all the receipts/deliveries of funds and securities. The statement shall also explain the retention of funds and securities and the details of the pledged shares, if any.

(c) On the date of settlement, the stock broker may retain the requisite securities/funds towards outstanding obligations and may also retain the funds expected to be required to meet derivatives margin obligations for next 5 trading days, calculated in the manner specified by the exchanges. In respect of cash market transactions, the stock broker may retain entire pay-in obligation of funds and securities due from clients as on date of settlement and for next day's business, he may retain funds/securities/margin to the extent of value of transactions executed on the day of such settlement in the cash market.

BSE Circular Notice No. 20210727-6 dated July 27, 2021:

"SEBI vide it email dated July 15, 2021 has advised Exchanges to issue guidelines to the trading members to make available the facility for online closure of trading accounts. The guidelines for online closure of trading accounts are enclosed as Annexure A. Further Trading members are also advised to inform their clients regarding the availability of facility for online closure of trading accounts and its guidelines through emails, SMS, weekly / fortnightly /monthly newsletters etc.

<u>*Guidelines for online closure of trading accounts*</u>

1. Client shall be entitled to close the trading account through online mode without giving any reasons to the trading member. Clients shall not be restricted from requesting, through online mode or offline mode, for the closure of trading account maintained with a member, subject to the compliance requirements as stipulated by SEBI / Stock Exchange from time to time.

2. Online request for closing of trading accounts shall be made available for the clients who have opened their accounts offline or online, by those trading members which provide facility of opening account online and provide various services to their clients in online *mode. Those trading members that do not provide any services online and do not open accounts online may not be required to offer online closure of trading accounts.*

Clause 2(B) of SEBI Circular CIR/MIRSD/15/2011 dated August 02, 2011:

2. *As an additional measure, it has now been decided in consultation with the major stock exchanges and market participants that the stock exchanges shall send details of the transactions to the investors, by the end of trading day, through SMS and E-mail alerts. This would be subject to the following guidelines:*

B. *Uploading of mobile number and E-mail address by stock brokers*

i. Stock exchanges shall provide a platform to stock brokers to upload the details of their clients, preferably, in sync with the UCC updation module.

ii. Stock brokers shall upload the details of clients, such as, name, mobile number, address for correspondence and E-mail address.

iii. Stock brokers shall ensure that the mobile numbers/E-mail addresses of their employees/sub-brokers/remisiers/authorized persons are not uploaded on behalf of clients.

iv. Stock Brokers shall ensure that separate mobile number/E-mail address is uploaded for each client. However, under exceptional circumstances, the stock broker may, at the specific written request of a client, upload the same mobile number/E-mail address for more than one client provided such clients belong to one family. 'Family' for this purpose would mean self, spouse, dependent children and dependent parents.

Rule 8(3)(f) of Securities Contract (Regulation) Rules, 1957:

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

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

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

Web-link of SEBI FAQ on Demat/Trading Account for minors dated September 25, 2018:

https://www.sebi.gov.in/sebi_data/faqfiles/may-2019/1558004460882.pdf

Schedule II (Code of Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992:

SCHEDULE II

Securities and Exchange Board of India (Stock Brokers) Regulations, 1992

CODE OF CONDUCT FOR STOCK BROKERS

[Regulation 9]

A. General.

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

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

Regulation 3.1.4 and Regulation 3.1.8 of Part A of Capital market Regulation of NSE:

3.1.4 *Trading Members may trade on the Trading System in securities that are admitted for dealing on the Exchange, either on behalf of their constituents or on their own account unless otherwise specified by the relevant authority and trading shall be subject to such conditions as the Exchange may prescribe from time to time.*

3.1.8 *Particulars of Unique Client Code*

When a Trading Member enters an order on behalf of a Constituent, then such a Trading Member shall at the time of entering orders on behalf of such Constituent, enter the unique code in respect of such Constituent in such format and with effect from such date as may be notified by the Exchange. Every Trading Member shall be responsible to furnish particulars of unique client codes of each of his Constituents to the Exchange in such form, manner, at such intervals and within such time as may be specified by the Exchange from time to time.

Regulation 3.1.19 of Regulations (F&O segment) of NSE:

3.1.19 *When a Trading Member enters an order on behalf of a Constituent, then such a Trading Member shall at the time of entering orders on behalf of such Constituent, enter the Unique Client Code in respect of such Constituent in such format and with effect from such date as may be notified by the Exchange. Every Trading Member shall be responsible to furnish particulars of Unique Client Codes of each of his Constituents to the Exchange in such form, manner, at such intervals and within such time as may be specified by the Exchange from time to time.*

Web-link of SEBI circular SEBI/HO/MIRSD/CIR/PB/2018/147 dated December 03, 2018:

https://www.sebi.gov.in/web/?file=/sebi_data/attachdocs/dec-2018/1543839622652.pdf#page=9&zoom=page-width,-16,563

Web-link of SEBI/HO/MIRSD/TPD/P/CIR/2022/80 dated June 07, 2022:

https://www.sebi.gov.in/web/?file=https://www.sebi.gov.in/sebi_data/attachdocs/jun-2022/1654606353820.pdf#page=1&zoom=page-width,-15,842

Regulation 21 of Securities and Exchange Board of India (Stock Brokers) Regulations, 1992:

Obligations of stock-broker on inspection by the Board.

21. *(1) It shall be the duty of every director, proprietor, partner, officer and employee of the stock-broker, who is being inspected, to produce to the inspecting authority such books, accounts and other documents in his custody or control and furnish him with the statements and information relating to the transactions in securities market within such time as the said officer may require.*

(2) The stock-broker shall allow the inspecting authority to have reasonable access to the premises occupied by such stock-broker or by any other person on his behalf and also extend reasonable facility for examining any books, records, documents and computer data in the possession of the stock-broker or any other person and also provide copies of documents or other materials which, in the opinion of the inspecting authority are relevant.

(3) The inspecting authority, in the course of inspection, shall be entitled to examine or record statements of any member, director, partner, proprietor and employee of the stock-broker.

(4) It shall be the duty of every director, proprietor, partner, officer and employee of the stock broker to give to the inspecting authority all assistance in connection with the inspection, which the stock broker may reasonably be expected to give.

Note: For detailed/ complete text of the provisions, relevant Rules, Regulations and Circulars etc., may be referred.

8. Based on perusal of the material available on record, submissions of the Noticees and giving regard to the facts and circumstances of the case, I record my findings hereunder:

Issue I. Violation of the provisions of the Rules, SEBI Regulations and Circulars:

(a) Whether Noticee-1 has violated the provisions of the Rules, SEBI Regulations and Circulars as mentioned in para no. 2 hereinabove?

(b) Whether Noticee- 2, 3 and 4 have violated the provisions of the Rules, SEBI Regulations and Circulars as mentioned in para no. 2 hereinabove?

9. I note that multiple allegations have been levelled against the Noticees, thus for the sake of convenience and clarity, I shall deal with each of the allegations independently in the following paragraphs. I find the following 13 violations have been alleged against the Noticees:

A) Allegations w.r.t. stock reconciliation
B) Allegations w.r.t. stock mismatch alerts
C) Allegations w.r.t. monthly/quarterly settlement of funds
D) Allegations w.r.t. reporting and short collection of Margin
E) Allegations w.r.t. client registration process
F) Allegations w.r.t. net worth verification

G) Allegations w.r.t. verification of weekly holding statement

H) Allegations w.r.t. verification of UCC

I) Allegations w.r.t. member engaged as a principal or employee in a business other than that of securities involving personal financial liability

J) Allegations w.r.t. trading in minor's accounts

K) Allegations w.r.t. dealing with unregistered constituents

L) Allegations w.r.t. cyber security and cyber resilience

M) Allegations w.r.t. non co-operation with inspection team.

A. <u>Allegations w.r.t. stock reconciliation</u>:

10. SCN alleges that Noticee-1 decided to reconcile the back-office holdings of client's securities with stocks lying in DP accounts as on September 30, 2022 with respect to 3 ISINs, Quantity – 1,30,010.53, Value – Rs. 8,280. Out of the said total quantity of 1,30,000 shares pertain to Bohra Industries Ltd., which was listed on SME platform of NSE and trading was suspended by NSE w.e.f. December 29, 2021, remaining 10 pertains to Indian Link Chain Manufacturers Limited (ISIN: INE359D01016) and 0.53 pertains to Mutual Fund units viz. Nippon Life India. On account of the non-reconciliation of clients' accounts as mentioned above, it is alleged that the Noticees violated the provisions of Clause 2.3 of SEBI Circular MRD/DoP/SE/Cir-11/2008 dated April 17, 2008.

Reply of Noticees

11. With respect to allegations of non-reconciliation of clients' securities, Noticees *inter alia* submitted the following:

(a) Out of the 3 instances, 1 instance of 1,30,000 shares is that of own account pertaining to Bohra Industries Ltd (listed on NSE SME Platform and suspended from trading w.e.f. December 29, 2021). Thus, the difference in respect of clients is merely on 2 instances of 10.53 shares/units, wherein 10 shares pertain to Indian Link Chain Manufactures Limited and 0.53 pertains to Mutual Fund units viz. Nippon Life India, totaling to amount of Rs. 8,280/-.

(b) W.r.t. difference of 1,30,000 shares pertaining to Bohra Industries Ltd pertains, Noticees submitted as under:

- The said 1,30,000 shares pertained to Stock Broker's own account only.
- The reason for difference as per DP statement and Stock Broker's books was due to Corporate Action on part of the Company on July 25, 2022 wherein there was 100% capital reduction.
- The said Corporate Action was not taken into account in Stock Broker's books as there was no mechanism for auto updating of Corporate Action and the same was reported to software vendors.
- Pursuant to the aforesaid, Stock Broker has made it a point to practice manual reconciliation of Corporate Actions at the end of every day.

(c) W.r.t. difference of 0.53 shares pertaining to Mutual Fund units viz. Nippon Life India, Noticees submitted that the fractional units were accumulating on daily basis over a period of time. Therefore, the same did not reflect in its books of accounts on September 30, 2022.

(d) W.r.t. difference of 10 shares of India Link Chain Manufactures Limited, Noticees submitted that Rikhav received payout on September 28, 2022 and the same was given to client on September 29, 2022. However, the aforesaid update was pending in the books as on September 30, 2022.

(e) Noticees further submitted that on daily basis Stock Broker report around 250-300 scrips. Thus, the differences in reporting of securities are miniscule both in terms of number and value. Pursuant to the investigation, till date there is no instance of differences in securities which are reported.

(f) Additionally, Noticees submitted as under:

- Vendor software was not updated to capture corporate actions on real time basis.
- The aforesaid observation is only in very few instances and value wise also there was no material impact.

- As on date, at the end of every day Noticees do stock reconciliation of our own stock with DP.
- Further, presently, there is no requirement w.r.t. reconciliation of client stock.

Findings

12. As per SEBI Circular MRD/DoP/SE/Cir-11/2008 dated April 17, 2008, stock brokers are required to maintain proper records of client collateral and the records should be periodically reconciled with the actual collateral deposited with the stock broker to prevent misuse of client collateral.

13. I note from the submission of Noticees that they have admitted that the securities of clients were not reconciled due to various reasons as mentioned above in para 11. I find that the justification given by the Noticees such as Corporate Action was not taken into account in Stock Broker's books as there was no mechanism for auto updating of Corporate Action, fractional units were accumulating on daily basis over a period of time etc. are not acceptable as Rikhav, being a registered Stock Broker, is required to have the necessary checks and balances to eliminate such omissions / lapses and should reconcile the securities of clients in timely manner to prevent any misuse of clients securities. Therefore, I hold that Noticee-1 has failed to reconcile the back-office holdings of client's securities with actual stocks lying in clients DP accounts as on September 30, 2022 with respect to said 3 ISINs (Quantity - 1,30,010.53 and Value - Rs. 8,280).

14. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Clause 2.3 of SEBI Circular MRD/DoP/SE/Cir-11/2008 dated April 17, 2008, stands established.

B. <u>Allegations w.r.t. stock mismatch alerts</u>:

15. SCN alleges that Noticees have incorrectly reported holding to the exchanges in 1 instance out of 20 samples as found in the inspection. Therefore, the Noticees were

alleged to have not complied with the provisions of Clauses 6.1.1(j) & 7.1.2 of SEBI Circular SEBI/HO/ MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016.

Reply of Noticees

16. In response to allegations of stock mismatch alerts, Noticees *inter alia* submitted the following:
    (a) The aforesaid incorrect reporting pertains to one client i.e. PJS01, where 15,000 shares were incorrectly reported instead of 1,500 shares of SBI. The aforesaid was a punching error. 1,500 shares of SBI were pertaining to withdrawal/ recall of stocks in Securities Lending & Borrowing Scheme (SLBS) segment for early Pay-in against client's obligation which is required to be entered manually in the back-office.
    (b) However, the said error was identified and subsequently rectified. Also, the pay-in and pay-out obligations of clients were being correctly processed. Noticees further submitted that the outward of the said 1,500 shares of SBI were shown correctly in demat account and in the Register of Securities. Noticees also furnished a copy of relevant extracts of demat account of PJS Securities LLP.
    (c) Further, Noticees submitted that they don't have software to import SLBM transactions as the same is very complicated by nature and very few clients were trading on this segment. So, Noticees were making manual entries in stock register of SLBM segment and doing reconciliation of client stock with DP, on daily basis. Noticees also submitted that as on date, there is no requirement to report stocks in client's accounts.

Findings

17. As per SEBI Circular SEBI/HO/ MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016, stock broker is required to upload the clients' fund balance and securities balance on Stock Exchange system. End of day securities balances (as on last trading day of the month) consolidated ISIN wise (i.e., total number of ISINs and

number of securities across all ISINs) is required to be submitted by the stock broker to the Exchange.

18. Noticees submitted 15,000 shares were incorrectly reported instead of 1,500 shares of SBI, and the said error was identified and subsequently rectified. Thus, I note that Noticees have accepted the allegation with respect to incorrect reporting of holding to the Exchanges.

19. Further, Noticees submission that they don't have software to import SLBM transactions as the same is very complicated by nature and they were making manual entries in stock register of SLBM segment cannot be accepted as Noticee-1 was required to furnish the correct end of day securities balances (as on last trading day of the month) consolidated ISIN wise (i.e., total number of ISINs and number of securities across all ISINs).

20. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Clauses 6.1.1(j) & 7.1.2 of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016, stands established.

C. <u>Allegations w.r.t. monthly / quarterly settlement of funds</u>:

21. It is alleged in SCN that settlement of 6 inactive clients was not done on quarterly basis and monthly settlement of funds was not done for 83 clients who had not traded in last 30 calendar days from the month of September 2021 onwards, as per SEBI guidelines applicable from the month of August 2021, which amounts to Rs. 28,04,215/-. Therefore, Noticees were alleged to have not complied with the provisions of Clause 12(e) of Annexure-A of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009 read with Clause 8.1 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016 and Clause no. 5.4. of SEBI circular SEBI/HO/MIRSD/DOP/P/CIR/2021/577 dated June 16, 2021.

Reply of Noticees

22. With respect to above allegations, Noticees *inter alia* submitted that the 6 instances were prior to introduction of SEBI circular dated June 16, 2021 which was applicable from August 31, 2021. The said clients were not traceable and the said funds were transferred to designated bank account.

23. In respect of the 83 instances, Noticees submitted the following:
    (a) In 3 instances, the clients' accounts were either settled or settlement requirement was not applicable. The settlement was done during the month for 3 clients for Rs. 1,89,698/-.
    (b) In 25 instances, pay-out was initiated but the same was rejected due to invalid bank details.
    (c) In 55 instances, clients' accounts were settled in subsequent months.
    (d) The instances of non-settlement are miniscule in terms of number and value considering the size of its operations. Also, it is pertinent to note that after introduction of the requirement since August 2021, it has improved its internal control in the said area.
    (e) Further, as on date there are no instances of non-settlement of non-active clients.

Findings

24. As per SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009, the actual settlement of funds and securities shall be done by the stock broker, at least once in a calendar quarter or month, depending on the preference of the client. Similarly, SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016 provides that the stock broker shall ensure that there must be a gap of maximum 90/30 days (as per the choice of client viz. Quarterly/Monthly) between two running account settlements. Further, SEBI circular SEBI/HO/MIRSD/DOP/P/CIR/2021/577 dated June 16, 2021 provides that for the clients having credit balance, who have not done any transaction in the 30 calendar

days since the last transaction, the credit balance shall be returned to the client by TM, within next three working days irrespective of the date when the running account was previously settled.

25. With respect to allegations of non-settlement of funds of 6 inactive clients on quarterly basis, Noticees submitted that these 6 instances were prior to introduction of SEBI circular dated June 16, 2021 which was applicable from August 31, 2021. I note that SEBI circular dated June 16, 2021 was issued in partial modification to aforesaid SEBI circular dated December 03, 2009 and circular dated September 26, 2016. As per SEBI circular dated December 03, 2009 and circular dated September 26, 2016, the actual settlement of funds was required to be done by Noticee-1 depending on the mandate of the client and there must be a gap of maximum 90 / 30 days (as per the choice of client viz. Quarterly / Monthly) between two settlements of running account. Further, Noticees submission that the said clients were not traceable and the said funds were transferred to designated bank account is not tenable as the settlement of funds of said 6 inactive clients was not initiated by Noticee-1 within the timelines prescribed. Thus, I hold that Noticee-1 has failed to settle the funds amounting to Rs. 2,17,601/- of said 6 inactive clients on quarterly basis.

26. With respect to allegations of non-settlement of funds of 83 inactive clients on monthly basis, Noticees submitted that in 3 instances, the clients' accounts were either settled or settlement requirement was not applicable. However, I note that Noticees have not stated that why the settlement requirement was not applicable to said 3 inactive clients. Further, I note that as per SEBI circular dated June 16, 2021 clients having credit balances, who have not done any transaction in the 30 calendar days since the last transaction, the credit balance was required to be returned to the clients within next 3 working days, however, Noticee-1 failed to do so. Thus, I hold that Noticee-1 has failed to settle the accounts of said 3 inactive clients amounting to Rs. 1,89,698/- on monthly basis.

27. In respect of non-settlement of funds at 25 instances, Noticees submitted that the pay-out was initiated but the same was rejected due to invalid bank details. I note that the settlement of funds of said 25 inactive clients was required to be initiated by Noticee-1 within 3 working days after clients have not traded in previous 30 calendar days. However, Noticee-1 initiated the settlement of funds of said clients through NEFT beyond the prescribed timelines. Thus, I hold that Noticee-1 has failed to settle the funds of said 25 inactive clients amounting to Rs. 14,79,071/- on monthly basis.

28. In respect of non-settlement of funds at 55 instances, Noticees admittedly submitted that the clients' accounts were settled in subsequent months. Thus, I note that Noticees have accepted the allegation that monthly settlement of funds was not done for said 55 clients who had not traded in last 30 calendar days from the month of September 2021 onwards. Hence, I hold that Noticee-1 has failed to settle the accounts of said 55 inactive clients amounting to Rs. 9,17,845/- on monthly basis in terms of the provisions of SEBI circular dated June 16, 2021.

29. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Clause 12(e) of Annexure-A of SEBI Circular SEBI/MIRSD/SE/Cir-19/2009 dated December 03, 2009 read with Clause 8.1 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016 and Clause no. 5.4. of SEBI circular SEBI/HO/MIRSD/DOP/P/CIR/2021/577 dated June 16, 2021, stands established.

D. <u>Allegations w.r.t. reporting and short collection of Margin</u>:

30. It is alleged in the SCN that Noticee-1 has done incorrect reporting of margins to the Stock Exchange. EOD margin shortfall in respect of 10 clients in 10 instances amounting to Rs.3,78,370.21/- was observed. Further, peak margin shortfall in respect of 8 clients in 8 instances amounting to Rs. 151131.74/- was observed. On account of the reporting of the margins, the Noticees were alleged to have not complied with the provisions of SEBI Circular No. CIR/DNPD/7/2011 dated August

10, 2011 read with Clause (iii) of Annexure to SEBI Circular No. SEBI/HO/MRD2/DCAP/CIR/P/2020/127 dated July 20, 2020.

Reply of Noticees

31. With respect to allegations of EOD margin shortfall in respect of 10 clients, Noticees *inter alia* submitted as under:

(a) 1 instance is for NRI client Hardik Jakharia (HXJ07) to whom EOD margin is not applicable.

(b) 6 instances for client codes VMl 12, VSS4, VSS5, VSSl, VG72 & VMl 10 (For EOD Margin and Peak margin). There was an OFS of Axis Bank on May 20, 2021 (Thursday) for Retail Category (value up to Rs. 2 Lakhs). All the clients transferred Rs. 2 Lakhs on May 19, 2021 and bided on May 20, 2021 and received the allotment for the same. However, due to some accounting error on its part, the client's ledger got debited on May 20, 2021. Rikhav came to know about the said error only on May 21, 2021 (late night) when client called for wrong debit entries. As May 21, 2021 was a Friday, Rikhav could give reversal credit of Rs. 28,49,715 only on May 24, 2021 i.e. on Monday. Therefore, only due to some accounting errors, the said ledgers generated margin shortfall EOD on May 21, 2021. There was no malafide intention on its part.

(c) Noticees further submitted that as per calculation, there are only 2 instances of incorrect EOD margin reporting amounting Rs. 49,143/-.

(d) The allegation is incorrect in calculation, the short margin already reported by Rikhav has not been considered.

(e) Noticees also stated that the Exchange has levied and collected EOD penalty for all 10 instances as stated above and furnished a copy of list of EOD penalty payment for these 10 instances.

32. With respect to allegations of peak margin shortfall at 8 instances, Noticees submitted as under:

(a) For 7 instances, Noticees reiterated their reply mentioned at para no. 31(a) and 31(b) hereinabove.

(b) All the above client's ledgers were in credit of Rs. 45,000/- on May 21, 2021 by EOD.

(c) Further, Noticees submitted that the Exchange has levied and collected EOD penalty for all 8 instances as stated above and furnished a copy of list of EOD penalty payment for these 8 instances.

(d) Noticees further submitted that the alleged incorrect reporting is very miniscule and therefore no adverse inference be drawn against them.

Findings

33. I note that SEBI Circular No. CIR/DNPD/7/2011 dated August 10, 2011 was issued with an intent of regular monitoring of and levying penalty for short-collection/ non-collection of margins from clients' in Cash and Derivatives segments. Further, as per SEBI Circular No. SEBI/HO/MRD2/DCAP/CIR/P/2020/127 dated July 20, 2020 the member shall have to report the margin collected from each client, as at EOD and peak margin collected during the day. And, higher of the shortfall in collection of the margin obligations w.r.t. EOD and peak margin shall be considered for levying of penalty as per the extant framework.

34. W.r.t. allegations of EOD margin shortfall in respect of 10 clients, I note that Noticees submitted that EOD margin is not applicable for 1 NRI client. Further, Noticees admittedly submitted that due to some accounting error on its part, the client's ledger got debited on May 20, 2021 for 6 clients and there were 2 instances of incorrect EOD margin reporting amounting Rs. 49,143/-. For remaining 1 instance Noticees have not made any submission, which indicates that Noticees have nothing to submit in this regard and the allegation levelled against Noticees is accepted by them. Thus, I note that Noticees have accepted the allegation that EOD margin in respect of 9 clients was reported incorrectly to the stock exchange.

35. W.r.t. allegations of peak margin shortfall at 7 instances, Noticees have reiterated their submissions mentioned at para 34 above. For remaining 1 instance Noticees have not made any submission, which indicates that Noticees have nothing to submit in this regard and the allegation levelled against Noticees is accepted by them. Noticees further submitted that the alleged incorrect reporting is miniscule and therefore no adverse inference be drawn against them. Thus, I note that Noticees have accepted the allegation of peak margin shortfall at 7 instances.

36. Noticees further submitted that the stock exchange has levied and collected penalty for EOD margin shortfall at aforementioned 10 instances and for peak margin shortfall at aforementioned 8 instances. I note that the stock exchange has levied and collected penalty for margin shortfalls under its regulatory provisions. However, for incorrect reporting of margins to the Stock Exchange, which is a violation of SEBI circulars, Noticee-1 ought to be penalised.

37. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of SEBI Circular No. CIR/DNPD/7/2011 dated August 10, 2011 read with Clause (iii) of Annexure to SEBI Circular No. SEBI/HO/MRD2/DCAP/CIR/P/2020/127 dated July 20, 2020, stands established.

E. <u>Allegations w.r.t. client registration process</u>:

38. With respect to client registration process, the following is alleged in SCN:

    (a) For Non-Mandatory Document: Noticee-1 has wrongly stated that the Running Account Authorization is also for settlement of securities, which is currently not applicable.

    (b) For Mandatory Document: Annexure for "DO's & Don't" contains the words "settlement of securities", which is also currently not applicable.

    (c) Member has not provided the facility of online closure of accounts on its website.

39. In view of the above, Noticees were alleged to have not complied with the provisions of Clause 13(b) and 13(c) of Annexure 6 of SEBI Circular CIR/MIRSD/16/2011 dated August 22, 2011 read with SEBI circular CIR/HO/MIRSD/DOP/CIR/P/2019/75 dated June 20, 2019; and BSE Circular Notice No. 20210727-6 dated July 27, 2021 read with Clause A(5) in Schedule II (Code of Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992.

Reply of Noticees

40. With respect to above allegations, Noticees *inter alia* submitted the following:

(a) Deletion of word "Settlement of Securities" is not prescribed in any of the SEBI and exchange circulars. Even though un-pledging or release of client securities is not required under present margin pledge system, the value of securities pledged is considered in calculating the amount of settlement.

(b) Irrespective of nomenclature, Rikhav has been following the procedure for settlement of client as prescribed in SEBI circular dated June 20, 2019 bearing reference no. CIR/HO/MIRSD/DOP/CIR/P/2019/75 on handling of client securities by TM/CM. Thus, in the light of expressed statutory requirements for settlement of securities prescribed above referred SEBI Circular, the word "Settlement of Securities" has become automatically ineffective.

(c) Taking cognizance of the said allegation, Rikhav has communicated to its clients vide email dated December 05, 2022 that the word "Settlement of Securities" referred to in Running Account Authorization and Do's and Don'ts of KYC stand deleted.

(d) In view of the above submissions, as the clause related to settlement of client securities has been ineffective.

41. W.r.t. allegations of not providing the facility of online closure of accounts on its website, Noticees submitted that for online closure of accounts, it has provided closure form on its website which the client is required to fill and send the same through email for closure of account. In absence of expressed process for online

account closure, Rikhav is following the above methodology, which is also followed by other Stock Brokers as well. Noticees also furnished a copy of snapshot of website showing account closure form.

Findings

42. SEBI Circular CIR/MIRSD/16/2011 dated August 22, 2011 prescribed the formats related to trading account opening to be followed by the stock brokers / trading members. Further, SEBI circular CIR/HO/MIRSD/DOP/CIR/P/2019/75 dated June 20, 2019 with respect to handling of client's funds and securities by stock brokers provides that TM/CM are required to transfer the clients' securities received in pay-out to clients demat account within one working day. It further stipulates that the provisions with regard to running account settlement of clients' funds and securities specified in SEBI Circulars MIRSD/ SE /Cir-19/2009 dated December 03, 2009 and SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016 shall stand modified and the said circulars shall be applicable only as guidelines for running account settlement of clients' "funds" only.

43. With regard to allegations of word 'Settlement of Securities' contained in Running Account Authorization and 'DO's & Don't', Noticees submitted that deletion of word "Settlement of Securities" is not prescribed in SEBI and exchange circulars. Rikhav has been following the procedure for settlement of client as prescribed in SEBI circular dated June 20, 2019. Further, Noticees submitted that taking cognizance of the said allegation, Rikhav has communicated to its clients vide email dated December 05, 2022 that the word "Settlement of Securities" referred to in Running Account Authorization and Do's and Don'ts of KYC stand deleted.

44. I note that SEBI circular dated August 22, 2011 prescribed the formats related to trading account opening and further SEBI circular dated June 20, 2019 states that previous circulars shall be applicable only as guidelines for running account settlement of clients' "funds" only. Thus, Noticee-1 should have modified the Annexure for "DO's & Don't" which contained the words "settlement of securities". Further, SEBI circular dated June 20, 2019 provides that TM/CM are required to

transfer the clients' securities received in pay-out to clients demat account within one working day. Hence, Running Account Authorization was also not applicable for settlement of securities. Therefore, considering the amended SEBI guidelines, Noticee-1 should have modified the Running Account Authorization format. I also note that SEBI circulars lays down the guidelines to be followed by the stock brokers and it may not always prescribe the deletion of words to be done by stock brokers. Stock brokers are expected to make the consequential changes to their forms/ undertaking based on the instructions, directions and guidelines prescribed under SEBI circulars.

45. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Clause 13(b) and 13(c) of Annexure 6 of SEBI Circular CIR/MIRSD/16/2011 dated August 22, 2011 read with SEBI circular CIR/HO/MIRSD/DOP/CIR/P/2019/75 dated June 20, 2019, stands established.

46. As per BSE Circular Notice No. 20210727-6 dated July 27, 2021, client shall be entitled to close the trading account through online mode without giving any reasons to the trading member. Online request for closing of trading accounts shall be made available for the clients who have opened their accounts offline or online, by those trading members which provide facility of opening account online and provide various services to their clients in online mode.

47. W.r.t. allegations of not providing the facility of online closure of accounts on its website, Noticees submitted that for online closure of accounts, it has provided closure form on its website which the client is required to fill and send the same through email for closure of account. I note that as per BSE circular, Noticee-1 was required to provide the facility of online closure of trading accounts through its website, however, Noticee-1 provided only closure form on its website and not the facility of online closure of accounts on its website. Therefore, I hold that the allegation that Noticee-1 has violated the provisions of BSE Circular Notice No. 20210727-6 dated July 27, 2021 read with Clause A(5) in Schedule II (Code of

Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992, stands established.

F. <u>Allegations w.r.t. net worth verification</u>:

48. It is alleged in the SCN that Noticee-1 has not considered the non-allowable assets while calculating net worth as a result of which net worth has reduced from Rs. 40.90 Crores to Rs. 40.72 Crores. Therefore, Noticees were alleged to have not complied with the provisions of Clause 6.1.1(j) of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016.

Reply of Noticees

49. With respect to above allegations, Noticees *inter alia* submitted the following:

(a) The non-allowable asset considered by the inspection team included (i) IPO Brokerage receivable (ii) Amount receivable from certain related parties and (iii) Advance given to Vendors totaling to 17.89 Lakhs which a miniscule amount of 0.44% of reported figure.

(b) In respect of Advance to vendors of Rs. 8,59,943/-, Noticees submitted that amount has been considered as non-allowable under the head of "Prepaid Expenses, Losses". However, Sr. No. 7 of Annexure -A of NSE Circular dated March 08, 2021 bearing reference no. NSE/COMP/47555 and Circular dated July 10, 2021 bearing reference no. NSE/COMP/48895 on clarification on net worth computation, the same does not prescribe any deduction for advances to vendors for net worth calculation. In fact, advance to vendors is not prescribed for deduction under any other head in the said Circulars.

(c) In respect of non-allowable assets of IPO brokerage receivable and receivable from certain related parties amounting to Rs. 9,29,531 /- Noticees further submitted the said amounts are not deducted but the same does not materially impact the net worth amount.

(d) Thus, effectively the variation is only 0.44% in total and 0.23% without considering the variation due to IPO brokerage receivable and receivable from certain related parties which are very miniscule.

(e) Further, net worth of Rikhav is 8 times the required net worth.

Findings

50. As per SEBI Circular SEBI/HO/ MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016, stock broker is required to submit the complete and correct data w.r.t. net worth to the Exchange.

51. In response to above allegations, Noticees submitted that the non-allowable asset considered by the inspection team included (i) IPO Brokerage receivable (ii) Amount receivable from certain related parties and (iii) Advance given to Vendors totaling to 17.89 Lakhs which a miniscule amount of 0.44% of reported figure. In respect of advance to vendors of Rs. 8,59,943/-, Noticees submitted that NSE Circular dated March 08, 2021 and Circular dated July 10, 2021 on clarification on net worth computation, does not prescribe any deduction for advances to vendors for net worth calculation. In fact, advance to vendors is not prescribed for deduction under any other head in the said Circulars.

52. In respect of non-allowable assets of IPO brokerage receivable and receivable from certain related parties amounting to Rs. 9,29,531/-, Noticees submitted the said amounts are not deducted but the same does not materially impact the net worth amount. Thus, effectively the variation is only 0.44% in total and 0.23% without considering the variation due to IPO brokerage receivable and receivable from certain related parties which are very miniscule. However, the net worth of Rikhav is 8 times the required net worth.

53. I note that the difference in net worth reported to the Exchange by Noticee-1 and actual net worth is miniscule and it does not materially impact the total net worth of Rikhav, which is well above the minimum required net worth. Thus, considering the

submissions of the Noticees, I am inclined to drop the allegations in favour of the Noticees.

54. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Clause 6.1.1(j) of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016, does not stand established.

G. Allegations w.r.t. verification of weekly holding statement:

55. SCN alleges the non-reconciliation of holding statement submitted by Noticee-1 with stocks lying in DP accounts as on September 30, 2022 - 3 ISIN, Quantity - 1,69,496.53, Value - Rs. 11,12,342.40. Therefore, Noticees were alleged to have not complied with the provisions of Clause 3 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016.

Reply of Noticees

56. With respect to above allegations, Noticees *inter alia* submitted the following:

(a) W.r.t. non-reconciliation of 1,30,000 shares pertaining to Bohra Industries Ltd pertains, Noticees reiterated their submission made at para 11 (b) hereinabove.

(b) Noticees submitted that the alleged deficiencies, if any as mentioned in the SCN, corrective and remedial steps have been taken post inspection and the lapses or deficiencies are no longer in existence.

(c) Additionally, for 39,496 shares, Noticees submitted that the said 39,496 shares pertain to G.K.P. Printing and Packaging Ltd held in its account. Bonus shares were received via corporate action on September 29, 2022, but the same got updated in its books only after September 30, 2022. Therefore, there is difference in DP account and its own account.

Findings

57. I note that SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016 provides for monitoring of clients' funds lying with the stock broker by the stock exchanges. It further provides that stock exchanges shall put in place a mechanism for monitoring clients' funds lying with the stock broker to generate alerts on any misuse of clients' funds by stock brokers.

58. With respect to allegations of non-reconciliation of holding statement with stocks lying in DP accounts, Noticees submitted that the corrective and remedial steps have been taken post inspection and the lapses or deficiencies are no longer in existence. Thus, I note that Noticees have accepted the violation with respect to the findings during inspection.

59. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Clause 3 of Annexure of SEBI Circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016, stands established.

H. <u>Allegations w.r.t. verification of UCC:</u>

60. It is alleged in SCN that single Email Id mapped to multiple clients- 27 Email Id against 75 clients and single mobile number mapped to multiple clients - 24 mobile number against 117 clients. Therefore, Noticees were alleged to have not complied with the provisions of Clause 2(B) of SEBI Circular CIR/MIRSD/15/2011 dated August 02, 2011.

Reply of Noticees

61. With respect to above allegations, Noticees *inter alia* submitted the following:

    (a) The said common Email ID and mobile number are that of Family members. The same is allowed vide Para 1 of NSE Circular dated May 31, 2016 bearing reference no. NSE/INSP/32471, wherein it is mentioned that *"......... The stock broker may, at the specific written request from client, upload the same mobile number/ E-mail address of one of the client's family member ".*

(b) Noticees furnished a copy of list of clients along with the relationship in case of mobile number and Email ID's, copies of sample letters received from clients belonging to the same family for common mobile number and for common Email Id’s.

(c) Noticees further submitted that as on date the KYC form itself has a provision to include common mobile no. and email id of the family members.

Findings

62. As per SEBI Circular CIR/MIRSD/15/2011 dated August 02, 2011, Stock Brokers shall ensure that separate mobile number/E-mail address is uploaded for each client. However, under exceptional circumstances, the stock broker may, at the specific written request of a client, upload the same mobile number/E-mail address for more than one client provided such clients belong to one family. ‘Family’ for this purpose would mean self, spouse, dependent children and dependent parents.

63. With respect to allegations of single Email ID and single mobile number mapped to multiple clients, Noticees submitted that the said common Email ID and mobile number are that of family members. In support of their claim, Noticees also furnished a copy of list of clients along with the relationship in case of mobile number and Email ID's, and copies of sample letters received from clients belonging to the same family for common mobile number and for common Email ID’s. Therefore, I am inclined to accept the submissions of the Noticees.

64. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Clause 2(B) of SEBI Circular CIR/MIRSD/15/2011 dated August 02, 2011, does not stand established.

I. <u>Allegations w.r.t. member engaged as a principal or employee in a business other than that of securities involving personal financial liability:</u>

65. It is alleged in SCN that Noticee-1 has invested in associate companies and has entered in an arrangement to borrow funds from client. It has also been alleged

that, Noticee-1 has entered into arrangement with arbitragers to extend loans, financing the securities transactions directly/indirectly, except as allowed for Margin Trading purposes. Therefore, Noticees were alleged to have not complied with the provisions of Rule 8(3)(f) of SCR Rules and NSE circular No. NSE/COMP/50957 dated January 07, 2022.

Reply of Noticees

66. With respect to allegations of investment in associate company, Noticees *inter alia* submitted the following:

(a) The associate company i.e. Rikhav Insurance Broker Private Limited ("RIBPL") was incorporated with an objective of carrying on the business of insurance broker but the business activities did not start.

(b) Rikhav's investments in RIBPL is from its own surplus funds. Further, Rikhav has not provided loan to RIBPL but invested in the equity shares of RIBPL, which is a private limited company. Its equity stake in RIBPL is only 20%.

(c) The said investment amount is already deducted while calculating the Net worth.

(d) Further, Noticees submitted that there is no bar in investing in listed or unlisted Pvt. Ltd companies.

67. In support of above submissions, Noticees placed their reliance on the following:

(a) Letter dated February 14, 2022 bearing reference no. SEBI/HO/MIRSD/DoP/P/OW/2022/6143/1 issued under SEBI (Informal Guidance) Scheme, 2003 in the matter of HDFC Securities Limited. Wherein, it is mentioned that interpretation of Rule 8(3) (1) of SCRR is that the Stock Brokers are not deemed to be engaged in business other than securities market as far as they do not incur any personal financial liability.

(b) Adjudication Order dated October 31, 2017 bearing reference no. EAD-12/AO/SM/95/2017-18 passed in the matter of inspection of Geojit BNP Paribas Financial Services Limited, which states that *"14 .... For any* *activity to be classified as business activity there should be several activities with several clientele......... "*.

"18. I note as per law there is no restriction on the inter corporate loans given by a SEBI registered intermediary. An inter-corporate loan given by a stock broker out of the surplus funds, which exceed the minimum net worth requirement applicable to stock broker as well as the working capital requirement for its business, as a temporary financial accommodation would not pose the risk to the business of the stock broker and affect the clients dealing with them. The main purpose of rule 8(3) {f) of SCRR was to prohibit the brokers to invest the clients' money in other businesses. However, in the present case, there is a clear demarcation of the clients' fund and its own fund. The loan that was advanced to GCPL was the excess fund of the Noticee. In no way was the fund of the client used to advance loan to the subsidiary. The clients' money was never exposed to any risk. The Noticee extended loans from its own excess funds".

(c) Order dated November 29, 2023 passed by Hon'ble Securities Appellate Tribunal (SAT) in the matter of Magnum Equity Broking Limited Vs. NSE (Appeal No. 461 of 2022). Relevant extract of the said Order is mentioned herein under:

"9. A plain reading of the Rule 8(3)(f} of SCR Rules and Rule S(b) of the Chapter II of the Rules of the Exchange would indicate that a trading member cannot engage as a principal or employee in any business involving any personal financial liability other than that of securities. SEBI's circular dated May 7, 1997 clarified that borrowing and lending funds by a trading member, in connection with or incidental to or consequential upon the securities business would not disqualify a trading member under Rule 8(3)(f} of the SCR Rules.

10. In its view, investment of surplus funds, generated as a consequence of securities business, with an NBFC registered with RBI cannot lead to an inference that the Appellant is engaged as a principal in business other than *that of securities involving personal financial liability. The Respondent Committee given a clear finding that the funds were advanced from the account of the Appellant therefore there is no dispute that the funds were their own moneys "*

68. Submission w.r.t. allegations of arrangement to borrow funds from clients:

(a) W.r.t. borrowing funds from Total Holdings and Finvest Private Limited ("Total Holdings"), Noticees submitted that Total Holdings is a NBFC registered with Reserve Bank of India and the funds have been borrowed under a separate loan arrangement for working capital purpose in the normal course of its broking business.

(b) Noticees further submitted that the allegation is merely on the grounds that Total Holdings, which has extended loan facility to Rikhav, is also its client. However, loan from NBFC and Member-Client relationship are two different things and should not be interlinked merely because both exist at the same time. As a client there is separate ledger account, separate bank account for pay in and pay out of funds and separate DP account is maintained for pay in and pay out of securities. Further, as a borrower too, there are separate bank account and ledger account maintained.

(c) Notably, funds have been borrowed for securities business and utilized for the same. Hence, SCRR Rules, Exchange Rules and NSE Circular dated January 07, 2022 bearing reference no. NSE/COMP/50957 cannot be said to be violated.

(d) The trading transactions, including pay-in, pay-out of Total Holding has taken place in a normal course of business like any other client and there is no impact on it due to the loan agreement. Hence, the loan transaction with Total Holdings is like any other transaction which an NBFC enters in its regular course of its NBFC activities and not otherwise.

(e) Rikhav has taken loan from Total Holding and not the other way round.

(f) In support of above submissions, Noticees relied on the on the Order dated February 15, 2024 bearing reference no. Order/BM/DS/2023-24/30022 passed by Ld. Adjudicating Officer, SEBI in the matter of Evermore Share Broking Private Limited, wherein it is mentioned that:

"24.4. I note that Noticee has parked its surplus funds and borrowed funds from Vayoo Nandan which is an NBFC. In view of the submissions made by the Noticee, there does not appear to be any violation as alleged."

69. Submissions w.r.t. allegations of arrangement with arbitragers to extend loans, financing the securities transaction:

(a) Submissions w.r.t. arbitrage activities carried out by Rikhav:

- Rikhav is engaged in doing jobbing and Arbitrage business with the help of the expert jobbers in its Proprietary Trading Account (Prop. Account).
- Arbitrage is a specialized skill which requires understanding of markets, research and movement of scrips over a period of time and spontaneity with presence of mind to buy and sell at the spur of the moment. Being a very specialized skill, the arbitragers are generally paid incentive. The incentive is determined after considering the transaction cost and cost of finance.
- In this regard, an agreement or Memorandum of Understanding (MoU) or Term Sheet is entered into them outlaying the Terms and conditions in respect of dealings or arrangement with them.

(b) Submissions w.r.t. agreements or MoU or Term Sheet (collectively known as Agreement) with arbitragers:

- Whenever an arbitragers/ jobber approaches, after all its due diligence, Rikhav take an appropriate sum of amount as interest free security deposits. In the agreement as submitted by it by letter dated December 07, 2022, it is mentioned that *"The Jobber shall simultaneously on the execution of this Agreement, deposit and keep deposited with the Company as and by way* *of interest free deposit for the entire period of this Agreement for the due observance and performance of the terms of this Agreement by the Jobber."*

- Rikhav is in charge of risk management, strategies to be adopted, guidance, training etc. The deposit so taken from them to ensure that they implement the strategy as given to them and adhere to the terms as agreed upon. The deposits are taken for its safety.
- Pursuant thereto, each arbitrager is allotted a specific exposure/limit as maybe mutually decided between Rikhav and the arbitragers/jobber. Rikhav also provide them with the required infrastructure, software for trading terminal, latest updated data etc. which helps them in better execution of trades.
- Arbitragers carry out their activities in its Proprietary Code. The overall supervision and control is with Rikhav.
- Rikhav is obligated to pay all margin monies to the stock exchange for the transactions carried out by its jobbers/arbitragers in its Prop account.

(c) Submissions w.r.t. charging of interest to arbitragers:

- The funds through which the arbitrager trades are from its own funds which are required to kept/reserved/available in Prop account and therefore interest is charged to them.
- Notional interest is charged as a component of cost of funds made available to the arbitragers for calculation of incentive to given to arbitragers. The notional interest component is a notional charge which is considered in calculation of incentive of each individual arbitrager as the same is not affected in books of accounts and thereafter incentive is provided to arbitrager.
- There is no loans or other financing the securities transactions are provided to the jobbers/ arbitragers.

(d) Noticees also stated that Rikhav has discontinued the practice of taking deposits from Arbitragers and it has returned deposits of all the arbitragers.

70. Noticees further submitted the following:

(a) The said investment, borrowing or arrangement, did not affect its net worth in any manner whatsoever.

(b) The investment was out of the surplus funds available with Rikhav.

(c) The said investment, borrowing or arrangement did not affect the client's dealings with Rikhav. The said investment was not out of client's funds but from its own surplus funds.

(d) The aforesaid instances did not possess risk to its business as "Stock Broker".

(e) SEBI circular dated May 07, 1997 inter alia states that *"……borrowing and lending of funds, by a trading member, in connection with or incidental to or consequential upon the securities business, would not be disqualified under Rule 8(1)(f) and 8(3)(f)".* Hence the said transactions are not disqualified under Rule 8(3)(f).

(f) The validity of circular dated January 07, 2022 bearing reference no. NSE/COMP/50957 which pertains to clarification to the Rule 8(1)(f) and 8(3)(f) of SCR Rules, which is the subject matter of present email September 18, 2024, is under challenge before the Hon'ble Bombay High Court in Writ Petition (L) No. 32739 of 2023 and said Writ Petition is admitted on July 24, 2024. The outcome of the said Writ Petition will have direct bearing on the subject matter of present proceedings.

71. Additionally, Noticees submitted as under:

(a) On similar subject matter, the Hon'ble SAT in the matter of Arihant Capital Markets Ltd Vs. National Stock Exchange of India Ltd. (Appeal No. 431 of 2023) has, vide Order dated 10.09.2024, stated as under:

“1. Learned advocate for the NSE submits that circular is under challenge before the Hon'ble Bombay High Court. Matter is adjourned sine die.... "

(b) Additionally, Ministry of Finance, Department of Economic Affairs, Financial Markets Division has issued Consultation Paper for Public Comments on Rule 8 of the SCRR. In the said Consultation Paper, it is proposed that the following rules be inserted:

2. In Rule 8 of the Securities Contracts (Regulation) Rules, 1957,

(i) in sub-rule(1), in clause (f), after the first proviso, the following proviso shall be inserted, namely:-

"Provided further that investment made by a member shall not be construed as business except when such investments involve client funds or client securities, or relate to arrangements which are in the nature of creating a financial liability on the broker."

(ii) in sub-rule(3), after clause (f), following proviso shall be inserted, namely:-

"Provided further that investment made by a member shall not be construed as business except when such investments involve client funds or client securities, or relate to arrangements which are in the nature of creating a financial liability on the broker."

Findings

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

73. With regard to violation of Rule 8(3)(f) of SCR Rules, Noticees submitted that investment in associate company, arrangement to borrow funds and entering into arrangement with arbitragers to extend loans, financing the securities transactions were carried out using its surplus funds and not out of client's funds. The said investment, borrowing or arrangement, did not affect its net-worth in any manner and it did not possess risk to its business as ‘Stock Broker’. Noticees have also

made references to SEBI Adjudications orders and Hon'ble SAT orders and High Court orders in their defense.

74. W.r.t. investment in associate company, I note that Noticee-1 has submitted that they invested its surplus funds in its associate company viz. RIBPL. In this regard I note that the networth of Noticee-1 was Rs. 40.89 Crore as on March 31, 2022 and its investment in RIBPL (its associate company) was Rs. 1.10 Crore as on March 31, 2022. In my view, the main purpose of rule 8(3)(f) of SCR Rules is to prohibit the brokers from investing clients' money in other businesses. However, in the present case, the said investment was not out of client's funds but from its own surplus funds. Thus, I am inclined to accept the submissions of the Noticees and drop the allegations in their favour.

75. W.r.t. borrowing funds from clients, I note from the submissions that Noticee-1 borrowed funds from 'Total Holdings', which is a RBI registered NBFC and the borrowed funds are under a loan arrangement for working capital purpose in the normal course of its broking business. In this regard, I note that SEBI vide Circular No. SMD/Policy/Cir-6 dated May 07, 1997, had clarified, inter alia, that borrowing and lending of funds by a trading member in connection with or incidental to or consequential upon the securities business would not be disqualified under rule/s 8(1)(f) and 8(3)(f) of Securities Contract (Regulations) Rules, 1957. In view of the same, there does not appear to be any violation as alleged.

76. W.r.t. allegations of arrangement with arbitragers to extend loans, financing the securities transaction, Noticees stated that Rikhav is engaged in doing jobbing and arbitrage business with the help of the Arbitragers/Jobbers in its Prop account after entering into agreement with them, which is in connection with or incidental to the securities business. Further, I note Rikhav has submitted that it has discontinued the practice of taking deposits from arbitragers and it has returned deposits of all the arbitragers. Therefore, I am inclined to accept the submissions of the Noticees in this regard.

77. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Rule 8(3)(f) of Securities Contract (Regulation) Rules, 1957 and NSE circular No. NSE/COMP/50957 dated January 07, 2022, does not stand established.

J. <u>Allegations w.r.t. trading in minor's accounts:</u>

78. It is alleged in SCN that Noticee-1 has allowed trading of securities in accounts of minor. Therefore, Noticees were alleged to have not complied in accordance with SEBI FAQ on demat/trading account for minors dated September 25, 2018 read with Clause A(2) in Schedule II (Code of Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992.

Reply of Noticees

79. With respect to above allegations, Noticees *inter alia* submitted the following:

(a) All this accounts were opened for investing in IPO's.

(b) In case of 12 instances, minors had already attained majority at the time of first trade.

(c) In remaining cases, the minor's trading accounts were opened for the purpose of sale of securities which were in minor's possession by way of IPO, inheritance, corporate action and off market transfers allowed in accordance with SEBI FAQ on demat/trading account for minors dated September 25, 2018. However, inadvertently since the buying limit was not restricted, trades got executed in the said minor accounts.

(d) However, pursuant to inspection, Rikhav has freezed the said minor trading accounts with immediate effect. Also, it has implemented necessary controls to ensure that minor accounts are not allowed to trade.

Findings

80. As per SEBI FAQ on demat/trading account for minors dated September 25, 2018, a minor cannot enter into a contract with a stock broker to purchase or sell any security. However, a trading account in the name of a minor can be opened only for the sole purpose of selling of securities possessed by the minor in the manner specified above.

81. In response to allegations of trading of securities in accounts of minors, Noticees submitted that in case of 12 instances, minors had already attained majority at the time of first trade. However, inadvertently since the buying limit was not restricted, trades got executed in the said minor accounts. Further, pursuant to inspection, Rikhav has freezed the said minors trading accounts with immediate effect. Thus, I note that Noticees have accepted the allegation of trading of securities in accounts of minors in respect of remaining 279 minor accounts.

82. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of SEBI FAQ on demat/trading account for minors dated September 25, 2018 read with Clause A(2) in Schedule II (Code of Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992, stands established.

K. <u>Allegations w.r.t. dealing with unregistered constituents:</u>

83. It is alleged in SCN that Noticee-1 is dealing with constituents who are not registered as clients on Exchange platform, taking funds from them in own account and trading on their behalf in Proprietary code. Therefore, Noticees were alleged to have not complied in accordance with Regulation 3.1.4 read with Regulation 3.1.8 of Part A of Capital market Regulation of NSE and Regulation 3.1.19 of Regulations (F&O segment) of NSE read with Clause A(5) in Schedule II (Code of Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992.

Reply of Noticees

84. With respect to above allegations, Noticees *inter alia* submitted the following:

(a) Adverse allegation of a serious nature like trading in own account through arbitragers using funds of constituents not registered with the exchange have been drawn against Rikhav merely on the basis of a single random complaint and its inability to provide agreement in a timely manner. In this regard, Noticees submitted that Rikhav is carrying out jobbing and arbitrage activities since more than past 25 years and this is the first ever complaint of such nature.

(b) The complainant, Mr. Thakkar was introduced to Rikhav by Mr. Ashish Mehta, its arbitrager and they were supposed to carry out jobbing activities jointly. As per its practice, Rikhav demanded a security deposit of Rs. 15 Lakhs for jobbing. The said deposit was paid jointly from the family members. Instead of crediting the amount to a single arbitrager deposit account of Mr. Thakkar, it was credited to individual account of the family members so that it is easy to identify the same at the time of returning the deposit. However, due to personal and professional difference between Mr. Mehta and Mr. Thakkar it was decided amongst them they will not work together. Mr. Ashish Mehta kept on pursuing Mr. Thakkar to discuss for settlement of their dispute as he was hopeful that the issues would be resolved by discussion. Meanwhile, Mr. Thakkar was insecure of the security deposit and thought that the funds have been mis-used by Mr. Ashish and therefore there is a delay in refunding the deposit. As a result, Mr. Thakkar, instead of approaching Rikhav, escalated the matter, resulting in the said complaint.

(c) The issues were discussed by Noticees in a joint meeting with Mr. Ashish Mehta and Mr. Kalpesh Thakkar. Mr. Thakkar agreed to withdraw the complaint when he was explained that Rikhav had no issue in refunding the said deposits. Rikhav had warned Mr. Ashish Mehta for delaying the refund of security deposit and as a goodwill gesture decided to settle the matter by paying a sum of Rs. 3.60 Lakhs. The sum so paid was ultimately recovered from Mr. Ashish by adjusting against his share of arbitrage. Hence, the conclusion of the inspection team that settlement was done due to some wrongdoing on its part is incorrect, baseless and based on assumptions as the settlement amount has been recovered by Rikhav.

(d) Further, Rikhav also has taken "No Dues Pending" letter dated October 17, 2022 from Mr. Kalpesh Thakkar. Rikhav has been unnecessarily dragged in the matter in the dispute between two of its arbitragers for no fault of its. It has discontinued the practice of taking deposits from arbitragers and it has returned deposits of 49 arbitragers.

Findings

85. As per Capital market Regulation of NSE and Regulations (F&O segment) of NSE, Trading Members may trade on the Trading System in securities that are admitted for dealing on the Exchange, either on behalf of their constituents or on their own account. Further, when a Trading Member enters an order on behalf of a Constituent, then such a Trading Member shall at the time of entering orders on behalf of such Constituent, enter the unique code in respect of such Constituent in such format and with effect from such date as may be notified by the Exchange. Every Trading Member shall be responsible to furnish particulars of unique client codes of each of his Constituents to the Exchange in such form, manner, at such intervals and within such time as may be specified by the Exchange from time to time.

86. In response to the allegations of dealing with constituents who are not registered as clients on Exchange platform, Noticees submitted that Mr. Kalpesh Thakkar was an arbitrager and Rikhav had entered into agreement with him. Noticees further submitted that the alleged amount of Rs. 15 Lakh was the security deposit paid by Mr. Kalpesh Thakkar and his family members as security deposit for jobbing/ arbitrage activities.

87. I note from the material available on records that an agreement was entered into between Rikhav and Mr. Kalpesh Thakkar for jobbing/ arbitrage activities. And as per the agreement Mr. Kalpesh Thakkar was required to pay the security deposit

to Rikhav. I also observe that the similar agreements were entered by the Rikhav with other jobbers/ arbitragers. These jobbers/ arbitragers were doing the jobbing/ arbitrage and funds were taken from them as a security deposit by Rikhav. Further, I also note the submissions of Rikhav that it has discontinued the practice of taking deposits from arbitragers and it has returned deposits of all the arbitragers. In view of the aforesaid, I am inclined to accept the submissions of the Noticees and drop the allegations in their favour.

88. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Regulation 3.1.4 read with Regulation 3.1.8 of Part A of Capital market Regulation of NSE and Regulation 3.1.19 of Regulations (F&O segment) of NSE read with Clause A(5) in Schedule II (Code of Conduct for Stock Brokers) of SEBI (Stock Brokers) Regulations, 1992, does not stand established.

L. <u>Allegations w.r.t. cyber security and cyber resilience:</u>

89. It is alleged in SCN that Noticee-1 has not obtained Standardization Testing and Quality Certification (STQC) for off-the-shelf products used by the member (Trading application and Back office application) for core business functionality. Therefore, Noticees were alleged to have not complied with the provisions of SEBI circular SEBI/HO/MIRSD/CIR/PB/2018/147 dated December 03, 2018 and SEBI/HO/MIRSD/TPD/P/CIR/2022/80 dated June 07, 2022.

Reply of Noticees

90. With respect to above allegations, Noticees *inter alia* submitted the following:

(a) Rikhav has not acquired or purchased the software. Rikhav is only users of the software on an annual license basis. The requirement for obtaining certification is in case off-the shelf products acquired or developed in house. Since Rikhav is not the owners of the said software, the requirement is not applicable to Rikhav.

(b) Noticees further submitted that front office trading software is approved by Exchange Empaneled vendor. Exchange has issued a circular requiring back-office vendor to register with the Exchange. Exchange has not made it mandatory for front office software to comply with STQC requirements before providing approval for the Front office software of Empaneled vendors or in house software of members.

(c) Further, it is not possible for Rikhav to apply and obtain the required certification. Also, there are no statutory guidelines prescribed by SEBI or Exchange requiring mandatory certification for back office and trading office software.

(d) STQC prescribed in the Cyber Audit reports are quality standards like ISO, COBIT etc. which are best business practices. In the absence of statutory requirements for adoption of standards, such standards are required to be adopted as per the business requirement, nature and size of operations.

(e) Noticees furnished the copies of certificate from Greeksoft Technologies Pvt. Ltd., Multitrade Softech Pvt. Ltd., 63 Moons Technologies Limited and Techexcel Software Solutions Pvt. Ltd for reference.

Findings

91. As per SEBI Circular SEBI/HO/MIRSD/CIR/PB/2018/147 dated December 03, 2018, Stock Brokers / Depository Participants should ensure that off the shelf products being used for core business functionality (such as Back office applications) should bear Indian Common criteria certification of Evaluation Assurance Level 4. The Common criteria certification in India is being provided by (STQC) Standardisation Testing and Quality Certification (Ministry of Electronics and Information Technology). Custom developed / in-house software and components need not obtain the certification, but have to undergo intensive regression testing, configuration testing etc. The scope of tests should include business logic and security controls.

92. In this regard, Noticees submitted that Rikhav is only users of the software on an annual license basis and the requirement for obtaining certification is in case off-the shelf products acquired or developed in house. Since Noticee-1 is not the owners of the said software, the requirement is not applicable to Rikhav. However, I note that the abovementioned SEBI Circular dated December 03, 2018 provides that off the shelf products being used by stock brokers for core business functionality (such as Back office applications) should bear Indian Common criteria certification of Evaluation Assurance Level 4 i.e. STQC. Thus, Noticee-1 was required to obtain the STQC for off-the-shelf products used by it (Trading application and Back office application) for core business functionality, however, it failed to obtain the same.

93. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of SEBI circular SEBI/HO/MIRSD/CIR/PB/2018/147 dated December 03, 2018 and SEBI/HO/MIRSD/TPD/P/CIR/2022/80 dated June 07, 2022, stands established.

M. Allegations w.r.t. non co-operation with inspection team:

94. It is alleged in SCN that Noticee-1 has failed to furnish the net worth related data viz. ageing for IPO brokerage receivable, Amount receivable from related party i.e. Rikhav IFSC and Rikhav Commodity and arbitragers/ jobbers agreements despite given sufficient time and multiple reminders. Therefore, Noticees were alleged to have not complied with the provisions of Regulation 21 of Securities and Exchange Board of India (Stock Brokers) Regulations, 1992.

Reply of Noticees

95. With respect to above allegations, Noticees *inter alia* submitted the following:

    (a) The inspection was jointly conducted by all the Exchanges and SEBI. It is possible that its team would have been occupied in providing information sought by the other Exchanges/SEBI resulting in delay.

(b) W.r.t. verification of net worth, Noticees further submitted state that the ageing was sought for IPO Brokerage receivable and receivable from certain related Parties totaling around Rs. 9,29,531/-. Since the amount of IPO Brokerage was not a party account, ageing was not readily available from the system. Further, the amount could not have any material bearing on the net worth and therefore there was no intention to conceal or hide information.

(c) W.r.t non-submission of copies of agreement of 54 arbitragers, Noticees stated that the same was not intentional or deliberate. Noticees further submitted that Rikhav had shifted to new premises just 2 days prior to the inspection. Hence, it was difficult to search for the documents. Therefore, the same could not be submitted at that point in time. However, the said agreements with 54 Arbitragers were submitted along with its reply dated December 07, 2022 which was filed in response to the findings of the inspection team.

(d) Additionally, below are certain reasons because of which there was delay in submitting the documents/ data:

- There were approximately 10 tasks between October 15, 2022 to November 30, 2022 that had to be completed as per Exchange Compliance calendar.
- Corporate Income Tax Return filing date was November 07, 2022.
- GST and TDS Returns filing due date was November 20, 2022.
- Also, the inspection was being done closer to Diwali and many of its support staff members were on holiday.
- As also stated aforesaid, Rikhav had shifted to new office premises just 2-3 days before the inspection commenced and Rikhav were finding it difficult to locate certain documents.

(e) In view of the aforesaid submissions, Noticees stated that it was never their intention not to co-operate with the inspection team, however due to certain circumstances beyond its control there was delay in submitting certain data and documents.

(f) The inspection of SEBI and other Exchanges coincided just prior to religious festival of Diwali. Hence, some of the concerned staff which was aware of the matter was on holiday.

(g) Further, all the documents/ data/ information was provided by its letter dated December 07, 2022. There is no allegation of not providing any documents/ information/data.

Findings

96. As per SEBI (Stock Brokers) Regulations, 1992, it shall be the duty of every director, proprietor, partner, officer and employee of the stock-broker, who is being inspected, to produce to the inspecting authority such books, accounts and other documents in his custody or control and furnish him with the statements and information relating to the transactions in securities market within such time as the said officer may require.

97. In this regard, above-mentioned submission of the Noticees is not acceptable as Noticee-1 being a registered stock broker is expected to have the necessary system and man power in place to effectively discharge its responsibilities as a stock broker and also to furnish the requisite data/ information during inspection. I note that Noticee-1 failed to provide the data regarding IPO Brokerage receivable despite multiple reminders given by inspection team. Also, the copies of agreements with 54 entities were not provided during inspection, which were furnished along with its reply dated December 07, 2022, i.e. 47 days after completion of the inspection. Hence, the justification given by the Noticees cannot be accepted. Thus, I hold that Noticee-1 had failed to furnish the net worth related data viz. ageing for IPO brokerage receivable, Amount receivable from related party i.e. Rikhav IFSC and Rikhav Commodity and arbitragers/ jobbers agreements despite given sufficient time and multiple reminders during inspection.

98. In view of the above, I hold that the allegation that Noticee-1 has violated the provisions of Regulation 21 of Securities and Exchange Board of India (Stock Brokers) Regulations, 1992, stands established.

(b) Whether Noticee- 2, 3 and 4 have violated the provisions of the Rules, SEBI Regulations and Circulars as mentioned in para no. 2 hereinabove?

99. I note that the SCN neither specifies the role of directors (Noticee 2, 3 and 4) of Rikhav with respect to the aforesaid violations alleged against them as mentioned in para 2 above nor provides the basis on which charges were alleged against them. Further, I note that the aforesaid violations as discussed in the preceding paragraphs have been committed by Noticee-1 who is responsible for compliance of the said provisions of SEBI Regulations, Circulars etc. In the absence of specific role of Noticee 2, 3 and 4 ascribed to them with respect to the alleged violations, I am of the view that the allegation that Noticee- 2, 3 and 4 have violated the provisions as mentioned in para 2 does not stand established.

Issue II. Does the violation, if any, attract monetary penalty under Section 15HB of SEBI Act, 1992?

100. In the light of the findings and observations made against the Noticees brought out in the foregoing paragraphs, it is evident that Noticee-1 has violated the regulatory provisions of SEBI Regulations, Circulars and other regulatory provisions as mentioned hereinabove.

101. With regard to levying of monetary penalty, Noticees have relied upon the observations of Hon'ble SAT in the matter of Religare Securities Limited Vs. SEBI (Appeal No. 23 of 2011), UPSE Securities Limited Vs. SEBI (Appeal No. 109 of 2011), M/s DSE Financial Services Limited Vs. SEBI (Appeal No. 153 of 2012) and Order in the matter of Akbar Badrudin Badrudin Jiwani V. Collector of Customs, Bombay AIR 1990 SC 1579.

102. In this regard, I note that the object of inspection of the books of accounts and records of any intermediary is to monitor the compliances and identify non-compliances, if any, with respect to process, procedure and systems prescribed through various provisions of the SEBI Act, 1992 and Regulations made thereunder and Circulars issued from time to time and thereafter, take necessary corrective steps for orderly, fair and transparent conduct of market participants. In the present case, I find from the observations made against Noticee-1 and other material available on record that Noticee-1 has failed to comply with the SEBI Regulations, Circulars and other regulatory provisions, hence needs to be dealt with suitable penalty.

103. Further, I find that the allegation of violations that were established in the cases relied upon by Noticee-1 are different from the violations that have been established in the present case of Noticee-1. Hence, I note that the said cases do not stand on the same footing as the given case of Noticee-1. I find from the findings made hereinabove and other material available on record that Noticee-1 has failed in performing its duties as a registered stock broker and also failed to adhere to high standards of services to its clients. Accordingly, such submissions of Noticee-1 are untenable. The aforesaid violations are serious in nature and make Noticee-1 liable for monetary penalty under the provisions of section 15HB of the SEBI Act, 1992.

104. In this regard, reliance is also placed upon the judgment of Hon'ble Supreme Court of India in the matter of **SEBI Vs. Shri Ram Mutual Fund** [2006] 68 SCL 216(SC) wherein it was *inter-alia* observed that: *"In our considered opinion, penalty is attracted as soon as the contravention of the statutory obligation as contemplated by the Act and the Regulations is established and hence the intention of the parties committing such violation becomes wholly irrelevant. A breach of civil obligation which attracts penalty in the nature of fine under the provisions of the Act and the Regulations would immediately attract the levy of penalty irrespective of the fact whether contravention must made by the defaulter with guilty intention or not.*"

105. With regard to issue of levying the monetary penalty on the Noticee- 2, 3 and 4, since the charges against Noticee 2, 3 and 4 have not been established, no monetary penalty is warranted on them. Accordingly, I hold that the charges levelled against Noticee 2, 3 and 4 in SCN dated April 19, 2024 are dropped without imposition of any penalty on them.

106. In view of the aforesaid, the aforesaid violations make Noticee-1 liable for penalty under Section 15HB of SEBI Act, 1992. The contents of the said provisions of law is reproduced herein below:

***SEBI Act, 1992*:**

Penalty for contravention where no separate penalty has been provided.

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

Issue III. If so, what would be the monetary penalty that can be imposed upon Noticee-1 taking into consideration the factors stipulated in Section 15-J of the SEBI Act, 1992 read with Rule 5(2) of the AO Rules?

107. While determining the quantum of penalty, it is important to consider the factors stipulated in Section 15-J of the SEBI Act, 1992, which reads as under: -

SEBI Act, 1992

Factors to be taken into account while adjudging quantum of penalty

15J *While adjudging quantum of penalty under 15-I or section 11 or section 11B, the Board or the adjudicating officer shall have due regard to the following factors, namely: —*

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

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

(c) the repetitive nature of the default.

[Explanation. —For the removal of doubts, it is clarified that the power to adjudge the quantum of penalty under sections 15A to 15E, clauses (b) and (c) of section 15F, 15G, 15H and 15HA shall be and shall always be deemed to have been exercised under the provisions of this section.]

108. In this case, from the material available on record, any quantifiable gain or unfair advantage accrued to Noticee-1 or the extent of loss suffered by the investors as a result of non-compliance to the provisions of the SEBI Regulations, Circulars and other regulatory provisions is not available. With respect to the repetitive nature of the default, I find that Noticee-1 was restrained from acting as syndicate/ sub-syndicate member for a period of four years, for being instrumental in inflating the bid book without any actual inflow of funds from the applications bid through its terminal and with the sole intention to falsely show a good response to the IPO, while acting in the capacity of a sub-syndicate member, *vide* WTM order dated August 5, 2014 in the matter of Vaswani Industries Ltd.

109. I note that the inspection findings bring out a number of instances where Noticee-1 has not been complying with the requirements of the SEBI (Stock Broker) Regulation, 1992, SEBI Circulars and BSE Circular as mentioned hereinabove. Noticee-1 was under a statutory obligation to abide by the provisions of the SEBI Regulations, circulars and other regulatory provisions, which it failed to do during the inspection period. The conduct of Noticee-1 in not complying with the provisions of SEBI Regulations, circulars and other regulatory provisions cannot be taken lightly. The violations by Noticee-1 are serious, therefore, should be dealt with by imposing monetary penalty as effective deterrence. However, while deciding the amount of penalty, I have also taken into account the number of instances and value involved in violations and corrective and remedial action taken by Noticee-1 post inspection.

ORDER

110. Considering all the facts and circumstances of the case including the submissions of the Noticees and findings elaborated hereinabove, the factors mentioned in 15J of the SEBI Act, 1992 and exercising the powers conferred upon me under Section 15-I of SEBI Act, 1992 read with Rule 5 of the AO Rules, I hereby impose a monetary penalty of ₹10,00,000/- (Rupees Ten Lakhs Only) under section 15HB of the SEBI Act, 1992 on Rikhav Securities Ltd (Noticee-1). In my view, the said penalty is commensurate with the violations committed by Noticee-1 in this case.

111. Noticee-1 shall remit / pay the said amount of penalty within 45 days of receipt of this order through online payment facility available on the website of SEBI, i.e. www.sebi.gov.in on the following path, by clicking on the payment link:

ENFORCEMENT → ORDERS → ORDERS OF AO → PAY NOW

112. In the event of failure to pay the said amount of penalty within 45 days of the receipt of this Order, recovery proceedings may be initiated under Section 28A of the SEBI Act, 1992 for realization of the said amount of penalty along with interest thereon, inter alia, by attachment and sale of movable and immovable properties.

113. In terms of Rule 6 of the AO Rules, copy of this order is sent to the Noticees and also to the SEBI.

Place: Mumbai **ASHA SHETTY**

Date: November 29, 2024 **ADJUDICATING OFFICER**