Member and Core Settlement Guarantee Fund Committee
("MCSGFC"/"Committee")
of
National Stock Exchange of India Limited
Exchange Plaza, Bandra-Kurla Complex, Bandra East, Mumbai – 400051
held on March 22, 2023

In the matter of the Trading Member
M/s. Motilal Oswal Financial Services Ltd.

CORAM:

Ms Mona Bhide	-	Chairperson
Mr K Narasimha Murthy	-	Committee Member
Mr S Ravindran	-	Committee Member
Mr Ranganayakulu Jagarlamudi	-	Committee Member
Mr Ashishkumar Chauhan	-	Committee Member

ALSO PRESENT:

Ms Priya Subbaraman	-	Chief Regulatory Officer
Dr Dinesh Kumar Soni	-	Senior Vice President – Regulatory
Ms Renu Bhandari	-	Vice President – Inspection
Mr Janardhan Gujaran	-	Vice President – Enforcement
Mr Shailesh Adukia	-	Vice President – Enforcement

BACKGROUND

1. **M/s Motilal Oswal Financial Services Ltd. ("Noticee")** is a Trading Member registered with the National Stock Exchange of India Limited **("Exchange"/"NSEIL")** and enabled for trading in the Capital Market **("CM")** segment since January 1995, Futures & Options **("F&O")** segment since January 2001, Currency Derivatives **("CDS")** segment since January 2013, and Commodity Derivatives **("COM")** segment since January 2013.

2. The Exchange conducted a regular inspection of the Noticee's books and records in October 2022, across the segments, covering the period from January 1, 2021, to December 31, 2021. Post-inspection, the Exchange issued a letter of observation dated October 17, 2022 **("LO-1")** to the Noticee for the observed non-compliances with the regulatory provisions. The Noticee, vide email dated November 17, 2022, replied to the LO-1.

3. The Exchange conducted a limited purpose verification of the Noticee's books and records during August 2022 to December 2022, covering the period from

February 1, 2022, to July 31, 2022. Post-verification, the Exchange issued a Show Cause Notice dated January 3, 2023 **("SCN")** to the Noticee for the observed non-compliances with the regulatory provisions. The Noticee, vide email dated January 16, 2023, replied to the SCN.

4. The Exchange conducted a limited purpose inspection of the Noticee's books and records in April 2022, across the segments, covering the period from April 1, 2022, to July 31, 2022. Post-inspection, the Exchange issued a letter of observation dated February 24, 2023 **("LO-2")** to the Noticee for the observed non-compliances with the regulatory provisions. The Noticee, vide email dated March 8, 2023, replied to the LO-2.

5. The above-mentioned matters were placed before the Committee in its meeting held on March 22, 2023.

INSPECTION OBSERVATIONS/VIOLATIONS

6. The observations/violations alleged in the LO-1, SCN and LO-2 are summarized hereunder:

LO-1

6.1. Non-collection of adequate margins in the form of cash, cash equivalent or Group I equity shares, with appropriate hair cut in 50 instances out of 400 instances, thereby constituting 12.5% of the total samples verified amounting to Rs.103.62 crores during the period from October 08, 2021, to November 23, 2021.

6.2. Incorrect reporting of margin collected from clients in the case of 1 instance (Client Code - DLS1020) out of 225 instances (0.4% of the total instances verified) involving Rs. 2.34 lakhs in the CD segment as on February 26, 2021.

6.3. Incorrect data submitted towards weekly monitoring of clients' funds in 2 areas involving Rs.0.02 Crore and Rs.338.48 crores as on December 31, 2021.

6.4. Incorrect data uploaded towards weekly holding statement in the case of 3 instances involving Rs.8.36 lakhs as on December 31, 2021.

6.5. Incorrect data reported towards weekly client level cash and cash equivalent balances in the case of 2 instances involving Rs. 2.90 lakhs as on December 31, 2021.

6.6. Non-maintenance of daily reconciliation statement for fund transfers between proprietary and client bank accounts in the case of 803 instances involving a net transfer from client bank account to own bank account amounting to Rs.8,365 crores.

6.7. Discrepancies in the maintenance of books and records.

6.8. Mismatch in email ids and mobile numbers uploaded to the Exchange in case of 192 instances and 184 instances respectively.

6.9. Delay in settlement of clients' funds in the case of 2 instances out of 100 instances (2% of the total samples instances verified) involving Rs.59,706/.

6.10. Discrepancy in the computation of net worth as of September 30, 2021.

6.11. Non-reporting of closure of 5 Demat accounts to the Exchange within one week of the closure.

SCN

6.12. Facilitating the financing of clients' transactions through a financier.

LO-2

6.13. Engagement as a principal in a business other than securities involving personal financial liability for the period from April 2022 to July 2022.

REGULATORY PROVISIONS

7. At the outset, it is appropriate to refer to the relevant regulatory provisions alleged to have been violated by the Noticee; extracts whereof are reproduced below:

LO-1

7.1. **Non-collection of adequate margins in the form of cash, cash equivalent or Group I equity shares, with appropriate haircut**

a. Exchange circular No. NSE/COMP/35125 dated June 15, 2017

Securities eligible for margin trading

3. Equity shares that are classified as 'Group I security' as per SEBI

Master Circular No. SEBI/HO/MRD/DP/C\|R/P/2016/135 dated December 16, 2016, shall be eligible for margin trading facility.

Margin Requirement

4. In order to avail margin trading facility, initial margin required shall be as under:

Category of Stock	*Applicable Margin*
Group I stock available for trading in the F&O Segment	*VaR + 3 times of applicable ELM**
Group I stock other than stocks	*Group I stock other than F&O stocks*

** For aforesaid purpose, the applicable VaR and ELM shall be as in the*
cash segment for a particular stock.

5. The initial margin payable by the client to the stockbroker shall be in the form of cash, cash equivalent or Group I equity shares, with appropriate hair cut as specified in SEB/ Master Circular No. SEBI/HO/MRD/DP/CIR/P/2016/135 dated December 16, 2016.

b. Exchange Circular No. NSE/COMP/48531 dated June 09, 2021

Q7. How initial margin shall be payable by clients to Member?

A. The initial margin payable by the client to the Member shall be in the form of cash, cash equivalent or Group I equity shares, with appropriate hair cut as specified in Section 1.1.3 of Chapter IV of SEBI Master circular No. SEBI/HO/MRD/DP/CIR/P/117 dated October 25, 2019 (previous SEBI circular SEBI/HO/MRD/DP/CIR/P/2016/135 dated December 16, 2016), and shall be recorded in the MTF books. The minimum initial margin required shall be as under: -

Category of Stock	*Applicable margin*
Group I stock available for trading in the F & O Segment	*VaR + 3 times of applicable ELM* Group I*
stocks other than F&O stocks	*VaR + 5 times of applicable ELM**

* *For aforesaid purpose, the applicable VaR and ELM shall be as in the*

cash segment for a particular stock.

Collateral in the form of securities under the margin trading facility shall be held by way of pledge only in terms of SEBI circular SEBI/HO/MIRSD/DOP/CIR/P/2020/28 dated February 25, 2020.

Members shall ensure that the initial margin is maintained for all the open funded positions as per the aforementioned prescribed rate at all times.

Q8. Can excess margin/collateral available in MTF ledgers be considered towards Margins of non-MTF transactions?

A. Excess margin/collateral available in MTF ledgers cannot be considered towards Margins of non-MTF transactions. However, in exceptional scenarios, transfers from non-MTF ledgers to MTF ledgers can be considered towards a margin position in MTF, provided they belong to the same clients and there are sufficient & free balances available in the non-MTF ledgers. Any transfer of balances from non-MTF ledgers to MTF ledgers undertaken with a view to avoid the actual settlement requirements will not be permitted. Further, any transfer of balances from non-MTF ledger to MTF ledger for MTF trades post confirmation of client will not be considered for computation of clear ledger balance till the settlement of trades. Members are requested to accordingly report the clear balances of the clients under weekly submissions of monitoring of client funds under Enhanced supervision guidelines of SEBI and Weekly submissions of Cash & Cash Equivalent balances to the Exchange.

7.2. **Incorrect reporting of margin collected from clients**

Exchange Circular No. NSE/INSP/43069 dated December 31, 2019

C. *Currency Derivative segment - In case of Currency Derivatives segment also, it is mandatory for Trading Members to collect initial margin, net buy premium and extreme loss margins from their client on an upfront basis. It must be ensured that all upfront margins are collected in advance of trade. The Mark-to-market losses shall be collected from clients by T+1 day. However, in case of currency future contracts, final settlement amount shall be collected by T+2 day.*

7.3. **Incorrect data submitted for weekly monitoring of client funds**

Exchange Circular No. NSE/INSP/33276 dated September 27, 2016

3.2. Stockbrokers shall submit the following data as on the 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.

7.4. **Incorrect data uploaded towards Holding Statement on a weekly basis**

a. Exchange Circular No. NSE/INSP/39393 dated November 13, 2018

Exchange shall seek periodic upload of day-wise Holding Statement in the specified standard format. The periodicity of reporting shall be weekly. Members have to submit the above mentioned data for all calendar days of that week on or before the next four trading days of the subsequent week. This circular shall be applicable with effect from January 1, 2019.

b. Exchange Circular No. NSE/INSP/46960 dated January 8, 2021

Exchange has provided certain additional clarifications in the revised format of cash & cash equivalent Balances and Holding Statement enclosed as Annexure-A and Annexure-B of this circular.

Members will have to submit the data for all calendar days of the week except Sunday on or before the next four trading days of subsequent week.

7.5. **Incorrect data reported towards weekly client level cash and cash equivalent balances**

a. Exchange Circular No. NSE/INSP/43926 dated March 23, 2020

1. *Day-wise upload of Client Level Cash & Cash Equivalent Balances on a weekly basis for all calendar days of that week except Sunday (i.e. Monday to Saturday);*

2. *Day-wise upload of bank Balances (as per the bank statement) of all bank accounts on a weekly basis for all the calendar days of that week except Sunday (i.e. Monday to Saturday)*

The aforesaid data / details shall be required to be submitted on or before the next four trading days of subsequent week.

b. Exchange Circular No. NSE/INSP/46960 dated January 8, 2021

Members will have to submit the data for all calendar days of the week except Sunday on or before the next four trading days of subsequent week.

7.6. **Non-maintenance of daily reconciliation statement for fund transfers between proprietary and client bank accounts**

Exchange Circular No. NSE/INSP/33276 dated September 27, 2016

2.4.2. *Transfer of funds between "Name of Stock Broker - Client Account" and "Name of Stock Broker - Settlement Account" and client's own bank accounts is permitted. Transfer of funds from "Name of Stock Broker - Client Account" to "Name of Stock Broker - Proprietary Account" is permitted only for legitimate purposes, such as, recovery of brokerage, statutory dues, funds shortfall of debit balance clients which has been met by the stock broker, etc. For such transfer of funds, stock broker shall maintain daily reconciliation statement clearly indicating the amount of funds transferred.*

7.7. **Discrepancies in the maintenance of books and records**

Exchange Circular No. NSE/INSP/38743 dated August 30, 2018

In order to standardize the maintenance of books of accounts / records and to ensure uniformity across all Members, a standard format for

register of securities, holding statement, bank book and client ledger is prescribed herewith.

The revised formats shall be applicable w.e.f. December 01, 2018. Members are advised to make necessary changes in their back office in order to comply with requirements.

Members may further note that non-maintenance of Register of Securities, Holding Statement, Bank Book and Client Ledger in the prescribed format is a violation of the provisions of the Securities Contracts (Regulation) Rules 1957 / Regulations of the Exchange and will attract appropriate disciplinary action as per Rule 1 and 2 of Chapter IV of NSEIL Rules.

7.8. **Mismatch in email ids and mobile numbers uploaded to the Exchange**

a. Exchange Circular No. NSE/INVG/21841 dated October 4, 2012

All Trading Members are requested to review the details of the clients uploaded on UCI Online pertaining to their mobile number and / or email address and update the same wherever necessary. Trading Members are hereby requested to take utmost care while uploading client details including mobile number and email address on UCI - ONLINE.

b. Exchange Circular No. NSE/INSP/32471 dated May 31, 2016

Separate mobile number/E-mail address shall be uploaded for each client. 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. 'Family' for this purpose would mean self, spouse, dependent children and dependent parents.

7.9. **Delay in settlement of clients' funds**

a. Exchange Circular No. NSE/INSP/13606 dated December 3, 2009

Unless otherwise specifically agreed to by a client, the settlement of funds/securities shall be done within 24 hours of the payout. However, a client may specifically authorize the stockbroker to maintain a running account subject to inter alia the following condition:

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.

b. Exchange Circular No. NSE/INSP/33276 dated September 27, 2016

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

c. Exchange Circular No. NSE/INSP/48624 dated June 16, 2021

5.1. The settlement of running account of funds of the client shall be done by the TM after considering the end of the day (EOD) obligation of funds as on the date of settlement across all the exchanges, at least once within a gap of 30 / 90 days between two settlements of running account as per the preference of the client.

5.4. 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.

7.10. **Discrepancy in the computation of net worth**

a. Schedule VI of Securities and Exchange Board of India (Stockbrokers) (Second Amendment) Regulations, 2013

The stockbroker shall have such net worth and shall deposit with the stock exchange such sum as may be specified by the Board/Stock Exchange for the relevant segment from time to time.

Explanation.- For the purposes of this Schedule, 'net worth' shall mean paid-up capital, free reserves and other securities approved by the Board from time to time but shall not include fixed assets, pledged securities, value of member's card, non-allowable securities (unlisted securities), bad deliveries, doubtful debts and advances (debts or advances overdue for more than three months or debts or advances given to the associate persons of the member), prepaid expenses, losses, intangible assets and 30% value of marketable securities.

b. Exchange circular no. NSE/INSP/48895 dated July 10, 2021

2. *Free Reserves*

As per Sec. 2(43) of the Companies Act, 2013, free reserves mean such reserves which, as per the latest audited balance sheet of a company, are available for distribution as dividend:

Provided that—

(i) any amount representing unrealised gains, notional gains or revaluation of assets, whether shown as a reserve or otherwise, or

(ii) (any change in carrying amount of an asset or of a liability recognised in equity, including surplus in profit and loss account on measurement of the asset or the liability at fair value,

shall not be treated as free reserves.

7.11. **Non-reporting of closure of demat accounts to the Exchange within the prescribed time**

Exchange Circular No. NSE/INSP/33276 dated September 27, 2016

2.3. Stock Exchanges and/or Depositories, as the case may be, shall ensure the following:

2.3.5. In case of closure of any of the reported bank and demat accounts, the same shall be communicated to the Stock Exchanges within one week of its closure.

SCN

7.12. **Facilitating financing of clients' transactions through a financier**

a. Exchange Circular No. NSE/INSP/6938 dated December 9, 2005

4.1 Trading members shall not be a party to any agreement or arrangement, directly or indirectly, entered into between their clients and any person including their subsidiary / holding company or group company, to fund the transactions executed by the trading members on behalf of their clients, or recognise or act

in accordance with any such agreement or arrangement entered into by the clients with any person.

4.2 Trading members shall not entertain, any instructions to trade in securities or transfer funds or securities, from any entity other than the clients, by prior arrangement or otherwise to facilitate financing clients' transactions.

4.3 Trading members shall not obtain any authorisation or power of attorney, for operating the depository and / or bank accounts of clients who avail financing facility for securities trading, conferring rights for operation of such accounts exclusively by the trading member.

4.4 Trading members shall not also otherwise finance or act as a conduit or front for financing any secondary market transactions entered into by their clients, directly or indirectly except in accordance with the regulatory provisions of Margin Trading Facility and Securities Lending and Borrowing.

b. Exchange Circular No. NSE/INSP/47278 dated February 9, 2021

Recently it has come to the notice of the Exchange that in order to fund the peak margin requirement of the clients, members have entered into arrangement with NBFCs for facilitating loan/credit facilities to the clients by NBFCs. Such financing arrangements are in violation of the SCRA/SEBI guidelines. In view of the same, members are again advised to ensure the following:

- *Trading members shall not be a party to any agreement or arrangement, directly or indirectly, entered into between their clients and any person including their subsidiary / holding company or group or associate company, to fund any secondary market transactions or margin requirements in respect of transactions executed by the trading members on behalf of their clients, or recognize or act in accordance with any such agreement or arrangement entered into by the trading members' clients with any person*

- *Trading members shall not entertain any instructions to trade in securities or transfer funds or securities, from any entity other than the clients, by prior arrangement or otherwise to facilitate financing of clients' transactions or margin requirements in*

respect of the transactions. Any financing arrangement with a general authorization by the clients are not permitted.

- *Trading members shall not otherwise finance or act as a conduit or front for financing any secondary market transactions or margin requirements in respect of the transactions entered into by their clients, directly or indirectly except in accordance with the regulatory provisions of Margin Trading Facility and Securities Lending and Borrowing.*

c. Exchange Circular No. NSE/INSP/52888 dated July 5, 2022

- *Trading Members shall not share transaction/obligation details of the clients with NBFC or any other lending institutions.*

- *Trading Members shall not engage in cross-selling of lending products or open joint (2 in 1 type of) accounts in collaboration with NBFC or any other lending institutions.*

LO-2

7.13. **Engagement as a principal in a business other than securities involving personal financial liability**

a. Rule 8(3)(f) of Securities Contracts (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.

b. SEBI Circular No. SMD/POLICY/CIR-6/97 dated May 7, 1997

It has been opined 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).

c. Exchange Circular No. NSE/COMP/50957 dated January 7, 2022

Members are not permitted to engage in any business or activities or transactions, directly or indirectly, other than that of securities or commodity derivative except as a broker or agent not involving any personal financial liability.

In consultation with SEBI and other Stock Exchanges, the illustrative list of activities that are construed as non-compliance to Rule 8(1)(f) and 8(3)(f) of SCRR, if undertaken by a member are provided as below:

9. Entering into any arrangement for extending loans or giving deposits / advances to any entity, including group companies such as subsidiaries & associates etc., not in connection with or incidental to or consequential upon the securities/ commodity derivatives business

10. Investments made in group companies such as subsidiaries & associates etc., not in connection with or incidental to or consequential upon the securities/ commodity derivatives business. (Ex: Investment in companies engaged in other businesses such as NBFC, Real Estate etc.)

PRESENT PROCEEDINGS BEFORE MCSGFC

8. The Exchange, vide its email dated March 15, 2023, granted the Noticee an opportunity for a personal hearing before the Committee in its meeting held on March 22, 2023.

8.1. On behalf of the Noticee, Mr. Ajay Menon – Designated Director and CEO, Mr. Shalibhadra Shah – CFO, Mr. Kailash Purohit – Company Secretary, Mr. Neeraj Agarwal – Compliance Officer, Mr. Ravichandra Hegde – Advocate and Authorized Representative, Mr. Ashish Venugopal – Advocate and Authorized Representative, and Mr. Samyak Pati – Advocate and Authorized Representative attended the personal hearing and made the following oral submissions before the Committee:

a. Engagement as a principal in a business other than securities involving personal financial liability

A clarificatory circular was issued by the Exchange bearing reference no. NSE/COMP/50957 dated January 7, 2022, wherein the investments in subsidiaries were discontinued to be permitted. Investments were made

during the period from 2013 to 2018 when there were no such regulations. Pursuant to the NCLT order in 2018, post obtaining due approvals of the Exchange for a merger, proper distribution of business was ensured. No active investment has been made post January 2022. Further, the funds in question are own surplus funds and do not belong to clients and there is no financial liability on the Noticee. Two entities in the observation wherein the investments are made are regulated entities which are listed and follow corporate governance practices. Status-quo of the previous investments which were done from F.Y. 2013 to 2018 is maintained.

b. <u>Facilitating financing of clients' transactions through a financier</u>

The Noticee has never been a party to the funding done by NBFC, having its own set of rules, regulations and RBI governing guidelines. Further, the decision of obtaining funding from an NBFC depends upon the client and not the Noticee. Motilal Oswal Finvest Limited **(''MOFL'')**, which is a subsidiary of the Noticee is also an NBFC, however, there is no connection between the operations carried on by MOFL as a subsidiary and an NBFC. The Noticee cannot be presumed to be a party to any agreement whereby MOFL, as an NBFC has provided funding to the Noticee's clients.

c. <u>Non-collection of adequate margins in the form of cash, cash equivalent or Group I equity shares, with appropriate hair cut</u>

Ideal funds of the clients lying in segments other than the Margin Trading Facility (MTF) segment, were utilized for reporting MTF margin also. The Noticee has now started segregating the funds and has started transferring the funds lying in other segments to the MTF segment.

8.2. Pursuant to the personal hearing and after considering the written submissions, the Committee directed the Noticee to provide the following documents:

a. Plan of action and schedule regarding the unwinding of investments by the Noticee in its subsidiaries including MOFL and Motilal Oswal Home Finance Limited **(''MOHFL'')**, which are not in connection with or incidental to or consequential upon the securities/commodity derivative business.
b. Plan of action to correct and streamline the prevalent systemic and operational issues of the Noticee.
c. Detailed write-up on the oral submissions made during the personal hearing and additional submissions, if any, along with relevant

supporting documents regarding the matters placed before the Committee.

The above directions were communicated to the Noticee vide Exchange email dated March 23, 2023.

8.3. The Noticee, submitted its response to the said email and the action plan vide its email dated April 6, 2023. The Noticee, in the action plan, submitted that it is contemplating a restructuring of its operations whereby the NBFC and Housing Finance Company would cease to be the subsidiary of the Noticee, which would require a National Company Law Tribunal approval process. Further, the indicative timeline for the mentioned re-structuring will be approximately 18 to 21 months.

CONSIDERATION & FINDINGS

9. The observations/alleged violations, the reply of the Noticee and the findings of the Committee are as under:

LO-1

9.1. **Non-collection of adequate margins in the form of cash, cash equivalent or Group I equity shares, with appropriate hair cut**

9.1.1. Upon verification of client MTF ledgers, MTF collateral details and MTF data available with the Exchange, it is observed that the Noticee has not collected adequate margin from its clients in the form of cash, cash equivalent or Group I equity shares, with appropriate haircut in case of 50 instances out of 400 instances(12.5% of the total samples verified) involving Rs.103.62 crores during the period from October 08, 2021, to November 23, 2021.

9.1.2. In reply to the LO-1, the Noticee submitted as under:

a. There are 10 unique customers in the Exhibit for which 50 instances of margin shortage for the MTF segment are observed by the Exchange. There was sufficient initial margin compliance at the time when the MTF position was taken by customers mentioned in the Exhibit.

b. Cash/non-cash collaterals for the MTF segment are incorrectly considered by the Exchange as there are certain unutilised collaterals available in the Non-MTF segment. The details of correct cash/non-cash collaterals for the MTF/Non-MTF

segment against all 50 instances and the resultant shortage are enclosed. Accordingly, there are shortages only in 13 instances (4 unique clients) out of 50 instances (10 unique clients) shared by the Exchange.

c. Further as per the Exchange guidelines dated June 9, 2021, on the MTF segment, Member may liquidate the securities if the client fails to meet the margin call made by the member as per the mutually agreed terms and conditions but not exceeding 5 working days from the day of margin call.

d. In the above 13 cases (4 unique clients), where shortages are observed, it is submitted that MTF shortages have not continued for more than 5 consecutive working days in 11 instances (unique 3 clients) and accordingly, the Noticee has complied with the Regulatory guidelines.

e. In case the shortages have been continued for more than 5 consecutive working days, the Noticee has the practice to liquidate the positions post margin call made to the client to ensure compliance with MTF guidelines.

f. A day wise shortage summary of these 3 customers depicting that shortage is not continued beyond 5 working days is submitted.

g. However, in 2 instances pertaining to 1 unique client (E513875), it is submitted that the said client was in shortage for consecutive 5 days, however, the Noticee had not taken RMS action as per the client's request.

9.1.3. The Committee finds as under:

a. The Noticee claimed that cash / non-cash collaterals for the MTF segment are incorrectly considered by the inspection team while arriving at the violation as there are certain unutilized collaterals available in the Non-MTF segment and if revised figures are considered, the violation will persist only in 13 instances pertaining to 4 clients.

b. In the case of 37 instances involving Rs. 85.84 crores, the Noticee has claimed to have free collateral available in the Non-MTF ledger for the said clients, and it has shared client ledgers (MTF/Non-MTF), DP Statements, MG-13 files (CM/FO/CDS) in

support of its claim. On verification of the client ledgers for 7 sample instances out of 37 instances involving Rs.37.65 crores, it is observed that the Noticee's claim is correct and hence, no violation persists.

c. In the remaining 13 instances, it is observed as follows:

i. <u>In case of 2 instances involving Rs. 1.16 crores</u>

The Noticee has accepted the inspection observation and stated that although the client margin shortfall continued for consecutive 5 days, they did not take RMS action as per the client's request since the clients' collaterals and stock was in profit. However, the Noticee's claim is not acceptable as the Noticee is supposed to maintain/collect the required margin from the client for all days. Hence, the violation persists.

ii. <u>In case of remaining 11 instances involving Rs. 16.61 crores</u>

The Noticee claimed that the margin shortage did not continue for more than 5 consecutive days. Upon verification of the file submitted by the Noticee consisting of total margin requirement along with cash and non-cash collateral available in the MTF segment and free collateral in the Non-MTF segment, it is observed that the said shortfall had not continued for more than 5 working days. However, the Noticee's claim is not acceptable as they are supposed to maintain/collect the required margin from the client on all days. Hence, the violation persists.

d. Therefore, post considering Noticee's submissions, the revised violation persists for 13 instances pertaining to 4 clients amounting to Rs.17.78 crores out of 400 instances verified, thereby constituting 3.25% of the total samples verified. The details of such 13 instances are as per the table below:

Sr. no.	Date	Client Name	Client Code	Required margin as per Exchange calculation(A)	Collateral value(B)	Shortage(A-B)
1	29-Oct-21	PALLAS FINCAP PRIVATE LIMITED	SAT3935	4,36,32,203.63	4,15,47,377.70	20,84,825.93
2	01-Nov-21	PALLAS FINCAP PRIVATE LIMITED	SAT3935	4,35,98,098.57	3,71,20,467.61	64,77,630.97

3	02-Nov-21	PALLAS FINCAP PRIVATE LIMITED	SAT3935	4,49,77,832.92	4,15,18,488.64	34,59,344.28
4	29-Oct-21	JAIKISAN RULIARAM AGARWAL	RH0116	10,58,66,521.70	2,55,43,658.96	8,03,22,862.74
5	02-Nov-21	JAIKISAN RULIARAM AGARWAL	RH0116	13,27,61,483.27	10,74,05,581.83	2,53,55,901.44
6	03-Nov-21	JAIKISAN RULIARAM AGARWAL	RH0116	10,61,05,351.43	10,46,74,147.97	14,31,203.45
7	04-Nov-21	JAIKISAN RULIARAM AGARWAL	RH0116	10,52,09,385.31	10,46,88,285.77	5,21,099.54
8	11-Nov-21	JAIKISAN RULIARAM AGARWAL	RH0116	12,83,25,620.39	9,98,73,407.53	2,84,52,212.86
9	18-Nov-21	JAIKISAN RULIARAM AGARWAL	RH0116	11,10,92,590.86	9,98,60,635.29	1,12,31,955.57
10	25-Oct-21	CHIRAG NARENDRA MODH	JEIP1308	3,47,87,712.68	3,14,85,439.22	33,02,273.46
11	26-Oct-21	CHIRAG NARENDRA MODH	JEIP1308	3,48,23,982.45	3,13,18,104.11	35,05,878.34
12	02-Nov-21	BHAGAVATULA ANNAPURNA KRISHNA PARMESWARI	E513875	2,72,41,821.48	2,42,48,244.47	29,93,577.01
13	23-Nov-21	BHAGAVATULA ANNAPURNA KRISHNA PARMESWARI	E513875	2,24,42,157.01	1,37,96,541.02	86,45,615.99
TOTAL						**17,77,84,381.58**

e. In the instant case, the Committee finds that by applying the matrix as set out in the Exchange Circular no. NSE/INSP/42919 dated December 16, 2019, the amount of penalty which becomes applicable in the present case is Rs. 88.05 lakhs, as per the calculation as explained below:

Sr. No.	**Particulars**	**Amount**
1	Amount of incorrect reporting	Rs. 17.77 crores
2	% of violations in the current inspection	3.25 %
3	Observed only in the current Inspection	Yes

4	Applicable Penalty as a percentage (%) of the False Reporting	5%
5	Penalty amount @ 5 % of Rs. 17.77 crores	Rs. 88.85 lakhs

f. Accordingly, the penalty leviable in accordance with the Exchange circular no. NSE/INSP/42919 dated December 16, 2019, is Rs.88.85 lakhs. However, the said Circular also stipulates that based on the slabs as provided in the said circular, the penalty amount for the non-collection of adequate margin, shall be capped at Rs.15,00,000/.

9.1.4. Given the findings mentioned above, the Committee decided to levy a monetary penalty of Rs.15,00,000/- in terms of Exchange Circular No. NSE/INSP/42919 dated December 16, 2019, and NSE/INSP/45533 dated August 31, 2020.

9.2. **Incorrect reporting of margin collected from clients**

9.2.1. Upon verification of the client ledger, cash margin ledger, collateral details and MG13 files, it is observed that the Noticee has reported incorrect margin collection from the clients to the Exchange in the case of 1 instance (Client Code - DLS1020) out of 225 instances (0.44% of the total instances verified) involving Rs.2.34 lakhs in CD segment as on February 26, 2021.

9.2.2. In reply to the LO-1, the Noticee submitted as under:

a. The observed client - Aditya Gupta having client code DLS1020 had a total EOD margin requirement of Rs.1.71 crore in CD segment on February 26, 2021, including an initial margin requirement of Rs.1.69 crore and MTM margin requirement of Rs.0.02 crore.

b. The Noticee had reported a margin collection of Rs. 1.68 crore (MTM of Rs. 0.02 crore and an initial margin of Rs. 1.66 crore and had reported a shortage of an initial margin of Rs. 0.03 crore.

c. With respect to the shortfall as observed by Exchange, it is submitted that the client had 32 different stocks which were considered for reporting. Out of them, the client had initiated a margin pledge request for 5,100 shares of Ashok Leyland

having ISIN INE208A01029 and 8,001 shares of Tata Motors having ISIN INE155A01022 on February 25, 2021, which was completed on February 26, 2021.

d. Further, out of the above quantity, the client sold 5,000 shares of Ashok Leyland and 1,000 shares of Tata Motors on February 26, 2021. Early pay-in of these shares was done on March 1, 2021 (T+1 day).

e. Due to the above multiple activities of shares being pledged and sold on the same day, the system had erroneously considered the above stock as pool quantity instead of pledged quantity and hence, the securities valuation was done without considering haircut. Accordingly, the excess securities valuation was considered for margin reporting and less shortage was reported to the extent of Rs.2.34 lakhs.

f. It is reiterated that the error in reporting was only due to the haircut amount as the stocks were considered as pool stock and not the pledged stock as of date of reporting.

9.2.3. The Committee finds as under:

a. The Noticee has accepted the inspection observation and attributed the incorrect reporting of margin to the erroneous consideration by the system of the stock as pool quantity instead of pledged quantity and, the securities valuation was done without considering haircut. Thus, the violation persists.

b. As per Regulation 3.9 of NSEIL Regulations (CM Segment), and Regulation 3.10 of NSEIL Regulations (F&O and CD Segments), and Exchange Circular No. NSE/INSP/43069 dated December 31, 2019, the Trading Members are required to collect upfront initial margin from all the clients and report on daily basis details of such margin due and collected. The Noticee has therefore violated the regulatory provisions mentioned above by incorrectly reporting the margins collected from the clients to the Exchange.

c. Further, the Noticee is a repeat violator. The Committee had levied a monetary penalty of Rs. 15,00,000/- on the Noticee for the observed violation in the financial year 2020-21.

9.2.4. Given the findings mentioned above, the Committee decided to levy a monetary penalty of Rs.23,400/- (10% of Rs.2,34,413.10=Rs.23,441 rounded off to Rs.23,400/-) in terms of Exchange Circular No. NSE/INSP/42919 dated December 16, 2019.

9.3. **Incorrect data submitted for weekly monitoring of client funds**

9.3.1. Upon verification of the data submitted by the Noticee towards weekly monitoring of clients' funds under the Enhanced Supervision of Stockbrokers as on December 31, 2021, vis-à-vis the client bank account balances, collateral deposited with Clearing Corporation/Clearing Member, credit and debit balances of clients, own collateral, it is observed that the Noticee submitted incorrect data towards weekly monitoring of client funds under enhanced supervision of stock broker to the Exchange as on December 31, 2021, in the case of the following 2 areas :

a. Total end-of-day balance in all client bank accounts including settlement account involving Rs.0.02 Crore.
b. Collateral deposited with the Clearing Corporations and/or Clearing Member in the form of Cash and Cash equivalents involving Rs.338.48 crores.

9.3.2. In reply to the LO-1, the Noticee submitted as under:

a. With respect to the difference in total end-of-day balance in all client bank accounts amounting to Rs.0.02 crore, it is submitted as under:

i. The Noticee had erroneously reported the closing bank balance which included the balance of the uncleared amount as on January 1, 2022.

ii. Above mismatch in bank balance was noticed only in 3 out of 51 client/settlement banks considered as on December 31, 2021, for enhanced supervision reporting.

iii. The error in reporting was only because the activity of arriving at a clear bank balance is a manual process where the entire bank statement has to be scrutinised for any entries which are cleared after reporting date

and hence it has to be eliminated to arrive at clear balance.

iv. The actual bank balances were not affected and further, there is no impact on the 'G' calculation.

b. With respect to the difference in Collateral deposited with Clearing Corporations and/or Clearing Members in the form of Cash and Cash Equivalents amounting to Rs.338.48 crores, it is submitted as under:

i. The Exchange has considered 50% of bank guarantees (Rs. 336.95 crores) placed with Clearing Corporation under computations, while the Noticee has not considered the same while computing collaterals with the Exchange since these are own bank guarantees and reporting being done pertains to clients' funds.

ii. Remaining Rs.1 crore pertains to the security deposit and base capital, for which the Noticee is always guided by the Exchanges not to consider BMC and Security deposits in Enhanced supervision calculations and the same practice is followed across all Exchanges.

iii. The Noticee has changed its practice and it is now reporting all funded value of all Bank guarantees as available in capital files of the Exchange.

iv. The figures are reported on the lower side as own bank guarantees were not considered and there were no intentions to do incorrect reporting.

9.3.3. The Committee finds as under:

a. With respect to the difference in the total end-of-day balances in all client bank accounts including the settlement account involving Rs.0.02 crore, the Noticee accepted the inspection observation and attributed the incorrect reporting to erroneously reporting the closing bank balances including the uncleared amount. Thus, the violation persists.

b. With respect to the difference in collateral deposited with the Clearing Corporations and/or Clearing Members in the form of Cash and Cash Equivalents amounting to Rs.337.95, the Noticee has accepted the inspection observation and attributed the same for considering the 100% value of the Bank Guarantees (BG) and Base Minimum Capital (BMC) while computing the collaterals. Thus, the violation persists.

c. The Noticee submitted that it has now changed its practice and reporting only the funded portion of the BG as available in the capital files of the Exchange.

d. As per the Exchange Circular No. NSE/INSP/33276 dated September 27, 2016, the Stock Exchanges have put in place a mechanism for monitoring clients' funds lying with the stockbroker to generate alerts on any misuse of clients' funds by stockbrokers. The Trading Members should ensure to verify the data before submission to the Exchange. Thus, the Noticee violated the regulatory provisions mentioned above by reporting incorrect data for weekly monitoring of clients' funds to the Exchange.

9.3.4. Given the findings mentioned above, the Committee decided to levy a monetary penalty of Rs.1,00,000/- for the observed violation in terms of Exchange Circular No. NSE/INSP/47457 dated February 25, 2021.

9.4. **<u>Incorrect data uploaded towards weekly holding statement</u>**

9.4.1. Upon verification of weekly submission of holding statement, register of securities and Demat holding statements, it is observed that the Noticee has uploaded incorrect data towards the weekly holding statement in the case of 3 instances involving Rs.8.36 lakhs as on December 31, 2021.

9.4.2. In reply to the LO-1, the Noticee submitted as under:

a. It has reported 2008 ISIN and 20,015 records in the weekly holding statement as on December 31, 2021.

b. As per the set process, the Noticee takes holding data (DPC9 report) from CDSL Easi/Easiest facility for reporting purposes

to Exchanges. However, the observed 3 ISINs were not reflected in DPC9 report downloaded from the Easi/Easiest facility given by CDSL systems as on December 31, 2021. Hence, the same were not captured in the Noticee's reporting.

c. Therefore, non-reporting of the observed ISINs was not due to any error at the Noticee's end but they relied on the data fetched from depository systems for weekly holding reporting.

d. Clarification has been received from CDSL and hence, such error shall not be repeated in future.

9.4.3. The Committee finds as under:

a. The Noticee stated that the observed ISINs were not reflecting in DPC9 report downloaded from the CDSL facility and, it has also written an email to CDSL for the same. Upon verification of the documents submitted by the Noticee, its contention is found to be true. However, the Noticee failed to report the correct balances basis the actual holding in Demat account to the Exchange. Thus, the violation persists.

b. Exchange Circular No. NSE/INSP/39393, dated November 13, 2018, requires the Trading Members to upload day-wise Holding Statement in the specified standard format every week.

c. Exchange Circular No. NSE/INSP/46960 dated January 8, 2021, has provided certain additional clarifications in the revised format of the holding statement and further reiterated that the Members are required to submit the data for all calendar days of the week except Sunday on or before the next four trading days of subsequent week.

d. The Exchange monitors the details submitted by the Trading Members as a part of its regulatory supervision, and any incorrect submission, therefore, defeats the purpose of regulation. Any incorrect reporting for reasons whatsoever is neither permissible nor acceptable. Hence, the Trading Members must verify the data before submission to the Exchange.

9.4.4. Given the findings mentioned above, the Committee decided to warn the Noticee to ensure the non-recurrence of the observed violation.

9.5. **<u>Incorrect data reported towards weekly client level cash and cash equivalent balances</u>**

9.5.1. Upon verification of client level cash and cash equivalent submission, client ledgers, trial balances, demat holding statements and records of Clearing Corporation, it is observed that the Noticee has reported incorrect financial ledger balance 'A' in the case of 2 clients amounting to Rs. 2.90 lakhs as on December 31, 2021.

9.5.2. In reply to the LO-1, the Noticee submitted as under:

a. The Exchange has observed mismatch only in 2 out of 12.87 lakhs client records uploaded towards cash and cash equivalent reporting as on December 31, 2021.

b. In case of client where the difference is of Rs. 500/-, the said client was erroneously missed out in the reporting.

c. For the other client, the Noticee reported correct balance as per ledger statement.

9.5.3. The Committee finds as under:

a. In 1 instance involving Rs. 500 – The Noticee accepted the inspection observation and stated that the reporting was missed out erroneously. Hence, violation persists.

b. For 1 instance involving Rs. 2.99 lakhs – The Noticee claimed to have reported the correct ledger balance. Upon verification of the cash and cash equivalent file submitted by the Noticee for the week ended January 1, 2022, it was observed that the Noticee's contention is not acceptable. Thus, the violation persists.

c. In terms of the Exchange Circular No. INSP/NSE/46960, dated January 08, 2021, Trading Members must report the cash and cash equivalents balance to the Exchange for all calendar days of the week except Sunday on or before the next four trading days of the subsequent week. The said

Circular was put in place to enhance the level of monitoring. Hence, the Trading Members must verify the data before submission to the Exchange. Thus, the Noticee is found to be in violation of Exchange Circular No. INSP/NSE/46960, dated January 08, 2021.

9.5.4. Given the findings mentioned above, the Committee decided to warn the Noticee to ensure non-recurrence of the observed violation.

9.6. **Non-maintenance of daily reconciliation statement for fund transfers between proprietary and client bank accounts**

9.6.1. Upon verification of bank statements and bank books of clients' bank account and the Noticee's proprietary bank account, it is observed that the Noticee has not maintained daily reconciliation statement indicating the details of the funds transferred between client bank account and proprietary bank account in the case of 803 instances, as per the below details:

a. Transfer from client bank account to own bank account - 591 instances amounting to Rs.14,795 crores.

b. Transfer from own bank account to client bank account - 212 instances amounting to Rs.6,430 crores.

c. Net transfer between client bank account and own bank account – Rs. 8,365 crores.

9.6.2. In reply to the LO-1, the Noticee submitted as under:

a. Clause 2.4.2 of SEBI circular dated September 26, 2016, mandated the Trading Members to maintain daily reconciliation statements clearly indicating the amount of funds transferred between client bank account and own bank account.

b. In this regard, it is submitted that funds are transferred from own bank to client bank and vice versa only as per the prevailing regulatory guidelines. Further, as required by Enhanced Supervision guidelines, the Noticee does daily EOD reconciliation of funds transferred between various own, client and settlement banks across all banks by consolidating each and every fund transfer entry. The

final net amount is derived which indicates whether funds were transferred from own bank to client bank/settlement bank or vice versa on an overall basis.

c. Sample statements along with client wise balance which were also shared with the Exchange, are enclosed.

d. Further, there is no format specified by Exchanges/SEBI and hence, internal format was being devised and adhered to, which satisfies the above regulatory requirement.

e. Sample reconciliation made for fund transfer from Client to Own / vice versa along with justification is submitted.

f. Funds that need to be transferred from Client Bank account to Own Bank account pertains to recovery of brokerage / charges, earlier temporary funding made to the clients etc.

9.6.3. The Committee finds as under:

a. The Noticee has denied the inspection observation and submitted that the funds are transferred between own and client bank account only as per the prevailing regulatory guidelines, and they are maintaining daily reconciliation of funds transferred between various own, client and settlement banks across all banks. However, the Noticee has failed to provide instance-wise response for the observed instances indicating transfer pertaining to recovery of brokerage or charges or towards recovery of temporary funding made to the clients. Thus, in absence of any instance specific reply, the violation persists.

b. The Noticee's claim that there is no format specified by the Exchanges and/or SEBI is not acceptable. Clause 2.4.2 of SEBI Circular dated September 26, 2016, mandate the Trading Members to maintain reconciliation statements clearly indicating the amount of funds transferred from Client Bank to Own Bank and vice versa states that as under:

"Transfer of funds between "Name of Stock Broker - Client Account" and "Name of Stock Broker -

Settlement Account" and client's own bank accounts is permitted. Transfer of funds from "Name of Stock Broker - Client Account" to "Name of Stock Broker - Proprietary Account" is permitted only for legitimate purposes, such as, recovery of brokerage, statutory dues, funds shortfall of debit balance clients which has been met by the stock broker, etc. For such transfer of funds, stock broker shall maintain daily reconciliation statement clearly indicating the amount of funds transferred."

c. The Noticee has therefore violated Exchange Circular No. NSE/INSP/33276 dated September 27, 2016.

9.6.4. Given the findings mentioned above, the Committee decided to levy a monetary penalty of Rs.25,000/- for the observed violation in terms of Exchange Circular No. NSE/INSP/47457 dated February 25, 2021.

9.7. **Discrepancies in the maintenance of books and records**

9.7.1. Upon verification of the bank books and bank statements submitted by the Noticee, the following discrepancies were observed:

a. Mismatch between the closing balance of the bank book and bank statements – 126 instances.

b. Mismatch amount between bank book and bank statements is reconciled in bank reconciliation, however, the entries are 3 months old – 204 instances.

c. Inter transfers from the banks are not present in the bank list available with the Exchange – 8 instances.

d. There are no transactions in the bank books of multiple clients' bank accounts, however, there are transactions in the bank statements – 13 instances.

9.7.2. In reply to the LO-1, the Noticee submitted as under:

a. Exhibit wherein 126 cases were noted by the inspection team where balance as per bank book and bank statement, are not matching, it is submitted that all entries are already available in

the bank reconciliation statement. The bank reconciliation statement for all the banks mentioned in the exhibit highlighting these entries is enclosed.

b. 204 cases where the entries are 3 months old in the Bank reconciliation statement, it is submitted that all the banks observed are proprietary banks. 50 out of such 204 instances pertain to bank account 990650003206 for which an incorrect bank reconciliation statement was provided to the inspection team as the statement generated through the system contained certain extra entries which were already cleared. The correct bank reconciliation statement and the bank book are enclosed.

c. In the remaining cases, bank reconciliations are done through systems and hence, entries are knocked off by the system if there are mismatch in the amount. These are cases where the Noticee had paid funds which are received back with a difference. Hence, the system has not knocked off the entries and is standing in reconciliation, which usually are knocked off manually at year end after getting necessary revert from vendor/banks etc.

d. There are a few cases where Bank had deducted TDS amount for which the Noticee was required to submit TDS Certificate. Hence the entries were pending in the reconciliation statement. In March 2022, the Noticee submitted TDS (Tax Deducted at Source) certificate and the necessary credit is received and bank reconciliation statement is cleared.

e. With regard to inter-transfer bank entries is observed in the bank accounts, which are not in the bank list available with the Exchange, it is submitted that the Noticee has uploaded bank account No.000405131484 (Settlement Bank Account opened with ICICI Bank) under Enhanced Supervision. Also, the bank account was given in the bank list which the Noticee had provided to inspection team during the course of inspection. Further these entries mentioned in Exhibit are inter segment bank fund transfer entries through control of GA1207 which are executed in January 2022 (Inspection period is till December 31, 2021). The bank details are updated with Exchange within 7 days of bank account opening (i.e., on December 8, 2021) as per prevailing regulatory guidelines.

f. Regarding nil transactions in the bank book, it is submitted that in 10 out of 13 cases, the bank book has necessary entries which are updated in the bank statement. The Bank book for the inspection period is enclosed. Further, for the remaining 3 instances, entries are available in bank reconciliation statement, which is enclosed.

g. Above observations arose only due to the large number of bank books/statements reconciliations, which were to be provided to the inspection team in a short span of time.

9.7.3. The Committee finds as under:

a. Closing balances of bank books and bank statements do not match (126 instances) - On verification of the sample entries, it is observed that entries are reflecting in bank reconciliation, but the receipt and payment are pending for more than 3 months. It is further observed that the expired cheque is also reflecting in the Noticee 's reconciliation. Hence, the violation persists.

b. Mismatch amount between bank book and bank statement is reconciled in bank reconciliation, however the entries are more than 3 months old (204 instances) –

i. In the case of 50 instances out of 204 instances - Upon verification of revised bank reconciliation statement, the Noticee's contention is found to be true. Thus, no violation persists.

ii. In the case of 15 instances out of 204 instances - The Noticee accepted the inspection violation and submitted that the system has not knocked off the entries and are standing in reconciliation, which usually are knocked off manually at year end. Thus, the violation persists.

iii. In the case of 4 instances out of 204 instances - The Noticee accepted the inspection violation and attributed the same to the non-submission of TDS certificate, the bank has not given the effect of TDS to the Noticee as these entries are older than 3 months and the Noticee has not updated the bank with the required submission. Thus, the violation persists.

iv. In the case of remaining 135 instances, the Noticee has not submitted reply. Thus, in absence of specific reply, the violation persists.

c. Inter transfer from the bank which is not present in the bank list available with the Exchange (8 instances) – Upon verification of documents submitted by the Noticee, it is observed that the Noticee had opened the bank account on December 04, 2021, and the same was updated to the Exchange on December 08, 2021. Thus, no violation persists.

d. No transactions in the bank book, however, there are transactions in the bank statement (13 Instances) –

i. Upon verification of 10 bank books submitted by the Noticee, it is observed that in the case of 9 bank books, transactions were recorded in bank book. Thus, no violation persists in the case of 9 instances.

ii. In the case of 1 bank book, there are no transactions observed in bank book. Thus, the violation persists.

iii. In the remaining 3 bank books, the Noticee has submitted bank reconciliation statements. However, it failed to submit bank books in support of its claim. Further, all are "Proprietary/own accounts of the Noticee. Thus, the violation persists.

e. Exchange Circular No. NSE/INSP/38743 dated August 30, 2018, provided a standard format for register of securities, holding statement, bank book and client ledger to be maintained by the Trading Members. The Noticee has therefore violated the said regulatory requirement.

9.7.4. Given the findings mentioned above, the Committee decided to levy a monetary penalty of Rs.25,000/- for the observed violation in terms of Exchange Circular No. NSE/INSP/47457 dated February 25, 2021.

9.8. **Mismatch in email ids and mobile numbers uploaded to the Exchange**

9.8.1. Upon verification of back-office records of the Noticee and UCC database of the Exchange, it is observed that there are mismatches in the email ids and mobile numbers mapped to the clients as per the Noticee's back-office records and those uploaded on the UCC database of the Exchange. Further, multiple clients were mapped to a single mobile number. Details of the said mismatches are as follows:

a. Mismatch in email id – 192 instances
b. Mismatch in mobile number – 184 instances
c. Single mobile number mapped to multiple clients – 846 instances.

9.8.2. In reply to the LO-1, the Noticee submitted as under:

a. For mismatch in email ids in 192 instances

i. In 129 instances, the Noticee had provided the email id to the inspection team which is mapped in its back office during inspection and there is no mismatch.

ii. In 36 instances, clients are inactive / closed in the back-office records as well as UCC database.

iii. In remaining 27 instances, as on date, there are no mismatch since the Noticee has updated the email ids in UCC database as per its back-office records.

b. For mismatch in mobile number in 184 instances

i. In 125 instances, the Noticee had provided the mobile number to the inspection team which is mapped in its back office during inspection.

ii. In 16 instances, clients are inactive / closed in the back-office records as well as UCC database.

iii. In remaining 43 instances, as on date, there are no mismatch since the Noticee has updated the mobile number in UCC database as per its back-office records.

c. Mapping of single mobile number to multiple clients in 846 instances

i. The Noticee has uploaded mobile number of all active clients in UCC database of the Exchange based on information provided by the client either in account opening form or through modification.

ii. In 815 instances, Mobile numbers mapped to clients are confirming to the definition of family (Spouse, Parents, Children) and hence, they are correctly updated in client records.

iii. In 22 instances, the customer had not provided valid mobile number and hence, as per the earlier Exchange guidelines, the Noticee was required to update 6666666666 in mobile number field of UCC records. However, erroneously, the Noticee had updated the mobile number as 7666666666. 12 out of such 22 clients, are marked as inactive on account of ensuring compliance of six KYC attributes. In remaining 10 cases, as clients have updated correct mobile numbers, the Noticee has updated the same in UCC database as well as in its back office records.

iv. In remaining 9 instances, the Exchange provided same mobile number (9820793652) against one client code ZHN043. The Noticee confirms that this mobile number is unique and is not mapped to multiple client codes.

9.8.3. The Committee finds as under:

a. For mismatch in email ids in 192 instances

i. For 129 instances where the Noticee claimed that they have provided email id as per its back-office records. On verification of the records, it is observed that in the case of 46 instances, the Noticee updated email ids post inspection. However, post-inspection compliance does not absolve the Noticee from the violation already committed. Thus, the violation persists in the case of 46 instances.

ii. In 36 instances, where the Noticee claimed that the clients are inactive/closed in the back-office records as well as UCC database. On verification of the records, it is observed that one client is still appearing as active as per the Exchange UCC database.

iii. In the remaining 27 instances, the Noticee claimed that there are no mismatches since the Noticee updated the email ids in UCC database of the Exchange as per the back office, which is found to be correct. Thus, no violation persists in the case of 27 instances.

b. <u>For mismatch in mobile number in 184 instances</u>

i. For 125 instances where the Noticee claimed that it has uploaded mobile number as per its back-office records. On verification of the records, it is observed that in the case of 39 instances, mobile numbers are updated post inspection. However, post-inspection compliance does not absolve the Noticee from the violation already committed. Thus, the violation persists in the case of 39 instances.

ii. In 16 instances, the Noticee claimed that the client codes are inactive/closed in its back office as well as in UCC database of the Exchange is not acceptable as the same are updated post inspection. However, post-inspection compliance does not absolve the trading members from the violation already committed. Thus, the violation persists.

iii. In 43 instances, the Noticee's claim to have updated the mobile number in UCC is not acceptable as the same were updated post inspection. However, post-inspection compliance does not absolve the Noticee from the violation already committed. Thus, the violation persists.

c. <u>Mapping of single mobile number to multiple clients in 846 instances</u>

i. Upon verification of documents submitted by the Noticee it is observed that in the case of 814 instances, the Noticee has shared valid relationship. Thus, no violation persists in case of 814 instances out of 842 instances.

ii. In the case of 13 instances, the Noticee's claim that it has marked client as inactive and in the case of 10 instances the Noticee's claim that it has updated the mobile number in the Exchange UCC database is found to be correct. Thus, no violation persists in case of 23 instances.

iii. In case of remaining 5 instances, the Noticee claimed that mobile number was unique and not mapped to multiple clients. On verification of records, it is observed that UCC - ZHN043 was reflecting multiple times in the observation shared with the Noticee. Thus, there is no multiple mapping, and no violation persists.

d. There are 5 unique clients where the mismatch pertaining to both email id and mobile number is observed.

e. In terms of the Exchange circular no. NSE/INVG/21841 dated October 4, 2012, all Trading Members are requested to review the details of the clients uploaded on UCI Online pertaining to its mobile number and/or email address and update the same wherever necessary.

f. Further, in terms of the Exchange circular no. NSE/ INSP/32471 dated May 31, 2016, separate email id/mobile number should be uploaded for each client.

9.8.4. Given the findings mentioned above, the Committee decided to levy a monetary penalty of Rs.5,000/- (Rs.1,000/- per client x 5 clients) for the observed violation in terms of Exchange Circular No. NSE/INSP/47457 dated February 25, 2021.

9.9. **Delay in settlement of clients' funds**

9.9.1. Upon verification of client ledgers, bank books, weekly client level cash and cash equivalent submission, Exchange trade data along with margin and obligation data from Clearing Corporations of the Noticee and retention statements submitted by the Noticee, it is observed that the Noticee has delayed the settlement of the clients' funds in the case of 2 instances out of 100 instances (2% of the total samples verified) involving Rs.59,706/-.

9.9.2. In reply to the LO-1, the Noticee submitted that the delay in settlement in above 2 instances was due to minor operational

errors. However, the clients were settled in respective all quarters during the period of inspection.

9.9.3. The Committee finds as under:

a. The Noticee accepted the inspection violation and attributed the same to minor operational errors in its system. Thus, the violation persists.

b. The concept of monthly or quarterly running settlement of clients' accounts by the Trading Member as per client preference is incorporated in Exchange Circular No. NSE/INSP/13606 dated December 3, 2009, respectively, to instill greater transparency and discipline in the dealings between the clients and the stockbrokers.

c. Further, Exchange Circular No. NSE/INSP/33276 dated September 27, 2016, and NSE/INSP/48624 dated June 16, 2021, prescribes 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.

d. The Noticee has therefore failed in its responsibility to comply with the above-mentioned Exchange circulars.

9.9.4. Given the findings mentioned above, the Committee decided to warn the Noticee to ensure non-recurrence of the observed violation.

9.10. **Discrepancy in computation of net worth**

9.10.1. Upon verification of the net worth certificate submitted by the Noticee, certifying a net worth of Rs.337.78 crores as of September 30, 2021, vis-à-vis the trial balance and balance sheet, it is observed that the Noticee incorrectly considered free reserves and deferred tax liability, pledged securities, doubtful debts and value of marketable securities while computing the net worth. After considering the correct valuation, the net worth is reduced from Rs.337.78 crores to Rs.328.73 crores as on September 30, 2021.

9.10.2. In reply to the LO-1, the Noticee submitted as under:

a. Free reserves and deferred tax liability

Deferred tax liability which is considered separately by the Exchange is a part of free reserves as the same is created as unrealized tax on unrealized gain and hence, when considered together, do not have major difference. CA certificate to demonstrate that deferred tax liability is created for unrealised tax on unrealized gain of Rs.1,155 crores is enclosed.

b. Pledged Securities

the Noticee has adopted IND AS (Indian Accounting Standard) methodology of accounting and as per said methodology, the Noticee needs to book investment at fair value. Further, as per the Exchange circular on “Calculation of Net worth" dated July 10, 2021, value of pledge securities to be considered for calculating Networth shall be the value as recorded in the books of accounts, on the date of the computation of the Networth", which in the Noticee’s case is fair value. Accordingly, the Noticee has considered fair value of pledged securities of Rs.6.46 crores, whereas the Exchange has considered cost price of the securities of Rs.3.06 crores. As the pledged securities have to be reduced from the net worth computation, considering Rs.3.06 crores as per the Exchange methodology, net worth will be increased by Rs.3.4 crore.

c. Doubtful Debts

The Noticee has not deducted value of Rs.11.99 crores of “supply of service” while calculating Net worth, as this majorly consist of advance for expense, ageing of which is also less than 90 days. Guidelines mentions to reduce doubtful debts which are overdue for more than 3 months.

d. The Noticee has maintained required Net worth as per prevailing regulatory guidelines and also calculation is as per L.C. Gupta methodology and guidelines issued by the Exchanges.

9.10.3. The Committee finds as under:

a. Free reserves and deferred tax liability

As per the Exchange circular no. NSE/INSP/48895 dated July 10, 2021, it was clarified that, while computing Networth, free reserves should not include any amount representing unrealised gains, notional gains or revaluation of assets, whether shown as a reserve or otherwise. Further, the said circular has not specified any treatment of "deferred tax liability" Thus, the Noticee's claim that deferred tax liability is created for unrealized tax on the unrealized gain is not acceptable. Thus, the violation persists.

b. Pledged securities

The Noticee's contention that it has adopted IND-AS (Indian Accounting Standard) methodology and accordingly booked the investments at fair value is found to be correct. As per the Exchange circular no. NSE/INSP/48895 dated July 10, 2021, the value of pledged securities to be considered for calculating Networth at the value as recorded in the books of account. Thus, no violation persists.

c. Doubtful debts

The Noticee's contention that supply of service is not overdue for more than 90 days and is prepaid expenses and hence, the same is not considered while arriving at net worth is not acceptable. As per Exchange Circular no. NSE/INSP/48895 dated July 10, 2021, it is clarified that prepaid expenses need to be reduced from the net worth. Thus, the violation persists.

d. The Noticee has therefore violated Schedule VI of Securities and Exchange Board of India (Stockbrokers) (Second Amendment) Regulations, 2013, and by incorrectly reporting the net worth to the Exchange.

9.10.4. Considering that the net worth is above the minimum prescribed net worth, the Committee decided to warn the Noticee to henceforth compute the net worth as per Dr. L.C. Gupta's method.

9.11. **Non-reporting of closure of demat accounts to the Exchange within the prescribed time**

9.11.1. Upon verification of the demat accounts reported by the Noticee and demat statements submitted thereof, it is observed that the Noticee has not reported closure of 5 Demat accounts to the Exchange within one week of the closure.

9.11.2. In reply to the LO-1, the Noticee submitted as under:

a. The Noticee has a process of updating opening and closing of demat as well as bank account in 7 days on the Exchange portals as per regulatory provisions. With respect to delay in updation of closure of above mentioned 5 Demat accounts, it is submitted that in 2 out of 5 observed accounts, Demat accounts were wrongly opened and hence closed on the same date i.e., September 20, 2019. Hence, the same were not reported earlier. However, upon receipt of Exchange query and to ensure the compliance, the Demat accounts were reported in February 2021 with both opening as well as closing date.

b. 1 Demat account was non broking Demat account opened as per listing guidelines of the Noticee for buy back of securities. Demat account was closed post completion of buy back activities but inadvertently missed out to update closure of the same in 7 days.

c. 1 Demat account, the delay was on account of non-receipt of timely information from HDFC bank with respect to closure request. The Noticee had placed a closure request with Bank and the bank had closed the Demat account but did not update the Noticee with the status. Upon following up with the bank, it was noticed that the said Demat account is already closed and hence, there was a delay in updating closure.

d. The remaining 1 Demat account was already closed in 2019 and identified in 2021 post receipt of Exchange query and hence, to ensure the compliance, the said demat account was reported in February 2021 with both opening as well as closing date.

9.11.3. The Committee finds as under:

a. In 2 out of 5 cases (IN301862-10004587 and IN301862-10004595) – Since the accounts were opened and closed on the same date, benefit for the same can be extended to the Noticee and thus, no violation persists for the said accounts.

b. The Noticee accepted the non-reporting of closure of 3 Demat accounts within 7 days and submitted as under;

   i. 1 Demat account was a non-broking Demat account (12012200-00161670) whose closure was inadvertently missed out to be updated in 7 days.

   ii. 1 Demat account, (IN301151-12161920), there was a delay in receipt of confirmation from HDFC bank pertaining to the account closure request.

   iii. In the remaining 1 Demat account (IN300394-18624205), the account was closed in 2019, but was reported in February 2021 upon receipt of Exchange query.

c. Thus, the violation stands in the case of 3 Demat accounts.

d. Exchange circular no. NSE/INSP/33276 dated September 27, 2016, prescribes that the Trading Members have to communicate closure of any of the reported bank and demat accounts to the Stock Exchanges within one week of its closure. The Noticee has therefore violated the said Exchange circular.

9.11.4. Given the findings mentioned above, the Committee decided to levy a monetary penalty of Rs.5,000/- for the observed violation in terms of Exchange Circular No. NSE/INSP/47457 dated February 25, 2021. Further, the Noticee is warned to ensure non-recurrence of the observed violation and is also directed to report such details to the Exchange.

SCN

9.12. **Facilitating financing of clients' transactions through a financier**

9.12.1. Upon verification of the receipt and payment entries in the bank books of subsidiary company of the Noticee viz., Motilal Oswal Finvest Limited ("MOFL"), it is observed that MOFL made payments amounting to Rs.1,14,086.59 crores to 1,794 clients of the Noticee during the period from February 1, 2022, to July 31, 2022.

9.12.2. Upon further verification of fund ledgers of 42 clients submitted by the Noticee for the period from February 1, 2022, to July 31, 2022, it is observed that the receipt entries in client ledgers amounting to Rs.59,153.82 crores matched the payments made by MOFL to the clients of the Noticee, thereby indicating financing arrangements between MOFL and the clients of the Noticee.

9.12.3. Upon seeking clarification, MOFL confirmed that the outstanding exposure of MOFL to 12,414 clients of the Noticee is Rs.1,281.39 crores as of October 31, 2022.

9.12.4. In reply to the SCN, the Noticee submitted as under:

a. The Noticee and MOFL fall under the umbrella of the Motilal Oswal group catering to a wide range of services in the financial sector. The Noticee has approximately 33 Lakhs retail clients for its broking business and has generated revenue close to Rs. 1,359 Crores for the half year ended September 2022.

b. The lending business of the Motilal Oswal group is carried out through MOFL. MOFL is a non-deposit taking systematically important NBFC, registered with the Reserve Bank of India (“RBI”) under Section 45-IA of the Reserve Bank of India Act 1934. The NBFC registration no. of MFL is N-13.02276. Being a group entity, admittedly there are certain commonalities in the management of the Noticee and MOFL, by way of common directors. However, operationally, both entities run independent of influence from each other and towards its respective business objective of being a sustainable financial services entity

under the group. Furthermore, as on date, there are no common directors between the Noticee and MOFL.

c. In furtherance, MOFL carries out its fund raising for its NBFC business independently from the market inter-alia by way of commercial paper and non-convertible debentures. As of quarter ending September 2022, MOFL has a corpus of Rs.3,787 Crores which it has deployed in various investments as well as towards its lending activities. Details of deployment of funds of MOFL as of March 2022 and as of September 2022, are in the manner provided below:

Rs. in crores

Particulars	March 2022	September 2022
Investments	1215	1989
Loans	588	1351
Cash and bank	811	437
Other assets	18	10

d. MOFL's lending business comprises of various products such as (a) providing loan against shares, (b) flexi loan, (c) IPO funding, and (d) working capital demand loan. The lending business is strictly carried out as per the extant RBI guidelines pertaining to lending against shares and employs a holistic procedure for grant of loans, as stated below:

i. MOFL has 5 branches across India and client sourcing is through the said branches;

ii. MOFL carries out rigorous credit and risk assessment inter-alia by dedupe check, verification of client as a watch out investor or SEBI debarred client list or RBI caution list or willful default list, NSDL PAN Verification, CKYC, CIBIL (min > 600) and income proof, before any loan is sanctioned to a borrower;

iii. Prospective borrower of MOFL is required to submit documents inter-alia income tax return, Net Worth certificate, KYC documents, Bank PoA, DP PoA, post dated cheque, board resolution (if corporate client) for satisfying eligibility of loan;

iv. An agreement is executed between MOFL and borrower only for grant of loan.

v. MOFL verifies all the documents as per the checklist and activates the client account in its system for disbursement.

e. MOFL have pre-set internal controls for setting sanction limits for each borrower qua their net worth and income, as ascertained from the documentation provided at the time of seeking the loan by a prospective borrower and certain products such as flexi loans and IPO funding are currently capped at Rs. 10 Lakhs and Rs. 1 Crore respectively as per extant guidelines.

f. At the inception, it is submitted that the SCN does not indicate, specifically, the role of the Noticee regarding the violations alleged. It is submitted that as the core allegation levelled by the Exchange is that the Noticee has purportedly 'facilitated' the financing of its clients' transactions through a financier i.e., MOFL. However, nothing in the SCN speaks towards this alleged facilitation except to state that MOFL has lent to clients of the Noticee. Therefore, the Exchange, in the present SCN, appears to have proceeded on a presumption that the Noticee must have a role in its clients availing funding. Without prejudice to the same, the following submissions are being stated on the allegations levelled in the SCN.

g. The investors availing financing for their trading activities has not only been a market practice for several years but is also a permissible lending activity.

h. As NBFCs are under the purview of the RBI, lending against shares ("LAS") by NBFCs were earlier governed by RBI under prudential regulation applicable to all NBFCs. Subsequently, RBI vide its Circular DNBS (PD).CC.No. 408 /03.10.001/2014-15 dated August 21, 2014, formulated guidelines on LAS.

i. These guidelines, coupled with clarification issued by RBI vide its Circular DNBR (PD).CC.No.028/03.10.001/2014-15 dated April 10, 2015, govern the business of LAS, which activity is undertaken by both NBFCs and scheduled

commercial banks alike. As such, there was no bar on the investors to avail funding through loans by pledging their shares as it was economically viable to leverage investment with borrowings and availing instant liquidity from one's investment without selling them.

j. Insofar as trading members are concerned, direct funding of securities' transaction of its clients by a trading member is only permitted by SEBI with respect to Margin Trading Facility ("**MTF**"), in the cash segment only, vide SEBI Circular bearing reference no. SEBI/MRD/SE/SU/Cir-15/04 dated March 19, 2004. For providing MTF, a broker was only permitted to use its own funds or borrow from scheduled commercial banks and/or NBFCs regulated by RBI and no other source, and this stipulation continues to remain even after the comprehensive review of the modalities of MTF by SEBI vide its Circular bearing reference no. CIR/MRD/DP/54/2017 dated June 13, 2017. This manner of funding has been stipulated by SEBI as not being fund based activity by TM/CM and therefore, is not in contravention of Rule 8(1)(f) & 8(3)(f) of Securities Contracts (Regulation) Rules, 1957.

k. The upshot of the above is that the investors are free to finance their trading activities from NBFCs, however, trading members are to play no role in such arrangements and are precluded from entering into arrangements by themselves except in accordance with the regulatory provisions of MTF and Securities Lending and Borrowing.

l. MOFL is admittedly a wholly owned subsidiary of the Noticee. The total equity held by the Noticee in MOFL is Rs. 905 Crores. It is submitted that while the Noticee and MOFL are indeed group entities, however, both operate separately in their respective areas of business. It is trite law that in case of two entities being a holding and subsidiary, a subsidiary remains a separate legal entity, even in case of a wholly owned subsidiary.

m. MOFL carries out its own independent fund raising from the market to carry out its business activities. As stated above, besides its lending activities in various products, MOFL is also involved in investments across various funds and as of September 2022, has deployed more of its funds

towards investment than its lending business. Therefore, MOFL is not incorporated as a financier of the Noticee's clients but it is lawfully and legitimately exercising its right to carry on the business of an NBFC, independently from the broking business of the Noticee.

n. It is submitted that 'facilitation' would amount to direct involvement in the decision-making process of MOFL which is not the case herein. It is submitted that the Noticee plays no role in its clients obtaining / wanting to obtain financing from any NBFC, including MOFL, for their trading activities. Clients of the Noticee are free to secure funding for their trading activities and the Noticee cannot regulate source of funds, except to ensure it is not illegal, and obtaining financing from NBFC, even from MOFL, does not preclude the Noticee to extend its broking services to such clients.

o. It is submitted that, assuming for argument, that clients of the Noticee are advised about various funding options, however, the decision of the clients to do so with a group company is their own and there is no mandate to obtain financing only from MOFL. The same does not amount to financing or being party to any arrangement as:

    i. There is an element of remoteness between the operations of the two entities as there is no flow of funds from the Noticee to MOFL for financing its clients.

    ii. MOFL has an independent corpus of funds, completely independent and delinked from the Noticee, which is used by it towards its lending business.

    iii. The Noticee is not a party to any arrangement or agreement that a client may seek from MOFL or any NBFC to obtain funds. Any agreement to obtain financing is strictly between the client and the NBFC.

    iv. The Noticee does not act on instructions from the clients' lenders and maintains due compliance with its regulatory requirement to act on its client's instructions. The Noticee does not require nor does it obtain any general authorization or PoA to operate client's bank account or

Depository Participant account and strictly adheres to norms of handling client securities.

p. It is submitted that the only basis for the allegation of 'facilitation' in the present case is that review of ledgers of 42 clients revealed payments for which the funds originated from MOFL and that MOFL has granted exposure to 12,414 clients of the Noticee. These facts are not disputed by the Noticee, however, the same are myopically being relied upon to suggest that the Noticee is actively participating and facilitating client financing through its subsidiary. It is submitted that the Noticee had a client base of approximately 28.5 Lakhs retail clients and generated a total revenue of over Rs. 2,611 Crores as of March 2022. Presently, the Noticee has over 33 Lakhs clients and in comparison, thereto the clients having financing from MOFL represents 0.003% of its total client base.

q. The fact of the matter remains that several clients of the Noticee have simply obtained financing from MOFL, however, the same does not amount to 'facilitation' to allege violation of the Exchange Circulars. There is nothing improper about trading clients obtaining external funding, which is a permissible activity of an NBFC under the prescribed RBI guidelines, and the same cannot become a basis for alleging violation of the Exchange Circulars merely by drawing a liner correlation between the Noticee and MOFL, being group entities. Therefore, the allegations in the SCN do not have any merit.

r. It is therefore, submitted that a legitimate business activity of a registered and independently regulated entity i.e., MOFL, cannot be said to be coordinated, controlled and / or facilitated by another company i.e., the Noticee, simply on the basis of being group entities, merely for the purpose of framing an allegation under the SCN.

s. A bare perusal of Exchange Circular No. NSE/INSP/6938 dated December 9, 2005, reveals that it was originally issued to curb unscrupulous arrangements which may result in abuse of client securities by a trading member as a result of improper transfer to / from different entities. The same is clearly envisaged in the said circular as extracted below:

*3. Certain arrangements have come to the notice of the Exchange by which, **the securities and funds of a client are received / transferred by trading members routinely** from / to the accounts of different entities or the joint accounts of the client with the financier or its agents, or the **trading member operates the client's bank account and / or depository account, under a financing arrangement with a general authorisation by the clients**.*

t. Similarly, Exchange Circular No. NSE/INSP/47278 dated February 9, 2021, states that:

*Further, attention is also drawn to SEBI circular CIR/HO/MIRSD/DOP/CIR /P/2019/75 dated June 20, 2019 which states that **clients' securities lying with the TM/CM cannot be pledged to the Banks/NBFCs for raising funds, even with authorization by client** as the same would amount to fund based activity by TM/CM which is in contravention of Rule 8(1)(f) & 8(3)(f) of Securities Contracts (Regulation) Rules, 1957.*

*Recently it has come to the notice of the Exchange that in order to fund the peak margin requirement of the clients, **members have entered into arrangement with NBFCs** for facilitating loan/credit facilities to the clients by NBFCs. Such financing arrangements are in violation of the SCRA/SEBI guidelines.*

u. Furthermore, Exchange Circular No. NSE/INSP/52888 dated July 5, 2022, states that:

*However, it has come to the notice of the Exchange that **certain members are engaging in funding the clients' transactions** either directly or through NBFC *or other lending institutions.*

v. None of the above circumstances referred to have been alleged in the present SCN. It is, therefore, clear that the principal intent behind the Exchange Circulars i.e.,

protecting client funds and securities are not in violation by the Noticee.

9.12.5. The Committee finds as under:

a. The Noticee has denied the violation and submitted as under:

i. The Noticee is not a party to any agreement between the client and MOFL /other NBFC and trading members are to play no role in such arrangements.

ii. The Noticee neither arrange for grant of financing to any client nor provide joint service with MOFL or any other NBFC.

iii. The Noticee does not share client obligation details with MOFL for which clients have availed funding.

iv. There is no flow of funds from the Noticee to MOFL for financing clients.

v. The Noticee carries out fund raising for its business independently from market by way of commercial paper and NCDs.

vi. Hence, although several clients of the Noticee have obtained financing from MOFL, the Noticee has not "facilitated" such financing.

b. It is observed that MOFL is a wholly owned subsidiary of the Noticee. Hence the corpus used by MOFL in lending and investing is not only restricted to funds raised from commercial paper and NCDs but also includes the funds infused by the Noticee as a capital. Thus, any funds lent by MOFL to the clients of the Noticee tantamount to lending done by the Noticee whether directly or indirectly which is in contravention to below mentioned regulatory provisions:

Exchange circular no. NSE/INSP/47278 dated February 09, 2021, stipulates that the Trading members were advised not to indulge in the practice of financing the securities transactions. Further members were also advised to desist from acting as a conduit or front for financing any secondary market transactions entered by their clients, directly or

indirectly except in accordance with the regulatory provisions of Margin Trading Facility and Securities Lending and Borrowing.

Thus, as per above circular, the Noticee has acted as a conduit between its clients and its subsidiary, MOFL to fund secondary market transactions and margin requirements.

c. The Committee observed that the receipt entries of Rs.59,153.82 crores matched the payments made by MOFL to the 42 clients of the Noticee. Upon review of ledger statement of 1 client (UCC- ASTA0103) out of 42 clients on sample basis, it is observed that, on April 07, 2022, and April 13, 2022, the Noticee received Rs.42.35 crores and, Rs.42 crores respectively and on the same day the Noticee initiated the funds payout for the same amount. The Noticee has denied that it has not shared the client's obligation details with MOFL, however the Noticee has failed to clarify how MOFL was aware of the client's obligations and on whose instruction's, the Noticee initiated funds payout from the client's ledger. This clearly establishes that the Noticee has facilitated the financing transaction through a financier.

d. Exchange circular No. NSE/INSP/52888 dated July 05, 2022, stipulates that the Trading Members shall not share transactions/obligation details of the clients with NBFC or any other lending institution.

e. Thus, the Noticee has violated the above mentioned Exchange circulars.

9.12.6. Given the findings mentioned above, the Committee decided a) to levy a monetary penalty of Rs.5,00,000/- for the observed violation in terms of Exchange Circular No. NSE/INSP/47457 dated February 25, 2021 and b) direction to stop financing of client transactions through financier with immediate effect.

LO-2

9.13. **Engagement as a principal in a business other than securities involving personal financial liability**

9.13.1. Upon verification of the monthly regulatory report submitted by the Noticee for the period from April 2022 to July 2022, it is observed that the Noticee has engaged as a principal in a business other than securities involving personal financial liability. It is observed that the Noticee made investments in the following subsidiaries:

a. Motilal Oswal Finvest Limited **("MOFL")** as of July 31, 2022, amounting to Rs.905.35 crores.

b. Motilal Oswal Home Finance Limited **("MOHFL")** as of July 31, 2022, amounting to Rs.566.33 crores.

9.13.2. In reply to LO-2, the Noticee submitted as under:

a. The investments were originally made by the Noticee in MOFL and MOHFL respectively and these investments stood automatically transferred to the Noticee on approval of the scheme of Merger as per the NCLT Order. Approvals of merger was obtained from the Exchange and SEBI.

b. Moreover, the liability is limited to the investments done in the said companies and the Noticee has not assumed any personal or contingent liability and neither any corporate guarantees are issued to anyone on behalf of these said subsidiaries. Therefore, no liability can be attributed to the Noticee for the violation alleged by the Exchange.

c. MOFL and MOHFL are now considered as high value debt listed under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 and are required to follow high level of Corporate Governance norms which are applicable to listed companies. MOFL and MOHFL also have strong credit ratings and robust capital adequacy ratios.

d. All transactions of the Noticee with group companies are on an arm's length basis and are approved by the Audit Committee. Further, all material transactions are approved by minority shareholders i.e., approval of public shareholders other than

Promoters, Directors and KMPs. All related party transactions are also submitted to Stock Exchanges on half yearly basis.

e. Thus, any investment in subsidiaries is highly governed not only by rules and regulations framed by SEBI, as well as the Companies Act, 2013. The scope and ambit of 'borrowing and lending of funds by a trading member' was expanded by the Exchange in January 2022.

f. The intent and objective of the said Exchange circular was to ensure that the trading members engaged in the business of securities, do not enter into any unwarranted businesses like entering into loan agreements with clients/entities, collecting money in the form of deposit or otherwise by offering fixed/ guaranteed/periodic returns orally or in writing, etc., in contravention of SCRR. The said circulars were aimed at preventing misuse of client funds and to ensure that the same are not diverted by the trading members, for their own personal use.

g. Accordingly, above structure of the Noticee having various holding companies which are into both securities and non-securities business, is approved by various regulators and hence this structure is not in violation of rule 8(1)(f) & 8(3)(f). Further, the Exchange Circular has come into force with effect from January 2022 and thus, it should not have retrospective effect on the Noticee's structure, which is in compliance with prevailing law.

h. In the present case, as the investments presently held by the Noticee in MOFL and MOHFL respectively, were made by the erstwhile MOSL's own funds, there exists no question of any alleged violation of SCRR and/ or the SEBI 1997 Circular and/ or Exchange Rules and/ or Exchange Circular 1 and/ or NSE Circular 2 respectively.

i. The Noticee has sufficient funds to honour financial obligations towards its clients as well as the Stock Exchange and Clearing Corporation, as is amply evident from the mandatory disclosures made by the Noticee to Exchange.

j. It is important to note that these investments have been made from MOSL's own surplus funds. For the sake of completion and full disclosure, prior to the merger, the Noticee had made

certain investments in MOHFL. However, no further investments were made by the Noticee in MOHFL, subsequent to the merger.

9.13.3. The Committee finds as under:

a. The Noticee contended that, the Exchange circular has come into force with effect from January 2022 and thus, it should not have retrospective effect on the Noticee's structure, which is in compliance with the prevailing law.

b. The Noticee's contention is not acceptable as the Exchange circular no. NSE/COMP/50957 dated January 07, 2022, is a clarificatory circular to Rule 8(1)(f) and 8(3)(f) of Securities Contracts (Regulation) Rules, 1957 (SCRR, 1957). Further, the said circular was issued in reference to the provisions of SCRR, 1957, SEBI Circular No. SMD/Policy/Cir-6 dated May 07, 1997, and SEBI Circular No. CIR/MIRSD/4/2015 dated September 29, 2015, which are primarily observed to be non-complied with.

c. The Noticee further contended that investment is governed by the rules and regulations of SEBI as well as the Company Act. The intent and objective of the Exchange circular was to ensure that the Trading Members engaged in the business of securities, do not enter into any unwarranted businesses like loan transaction with clients/entities, collecting money in the form of deposit or otherwise by offering fixed/ guaranteed/periodic returns orally or in writing, etc., in contravention of SCRR and the investments were made from own surplus funds.

d. Rules 8(3)(f) of the Securities Contracts (Regulation) Rules, 1957 ("SCRR, 1957") imposes certain restrictions on activities of the Trading Members that the members of a Stock Exchange, 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.

e. Further SEBI Circular No. SMD/Policy/Cir-6 dated May 07, 1997, specified 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 Rules 8(1)(f) and 8(3)(f) of SCRR, 1957.

f. It is observed that as on July 31, 2022, the Noticee has investments in its subsidiary companies despite the Exchange in its clarificatory circular no. NSE/COMP/50957 dated January 07, 2022, reiterated that the investments made in group companies such as subsidiaries and associates etc., not in connection with or incidental to or consequential upon the securities/commodity derivatives business is not permitted. The said circular also provides examples indicating that investment in companies engaged in other businesses such as NBFC, real estate etc. will be construed as non-compliance to Rule 8 (1) (f) and 8 (3) (f) of SCRR, 1957.

g. Therefore, the Noticee has failed in its responsibility to comply with the above-mentioned regulatory requirements, by engaging as a principal in a business other than securities involving personal financial liability, the Noticee has violated the above-mentioned regulatory requirements.

9.13.4. Given the findings mentioned above, the Committee decided to (a) levy a monetary penalty of Rs.5,00,000/- for the observed violation in terms of the Exchange Circular No. NSE/INSP/47457 dated February 25, 2021; (b) direct the Noticee to submit a restructuring plan within 45 days from the date of this order pertaining to disinvestment and (c) submit quarterly compliance report for execution of action plan within 10 days from the end of the respective quarter.

10. In view of the above, the Committee levies the following penalties as indicated against each of the violations:

Sr. No.	**Committee's Findings**	**Prescribed penalty as per Exchange Circular No. NSE/INSP/42919 dated December 16, 2019, NSE/INSP/45533 dated August 31, 2020, NSE/INSP/47457 dated February 25, 2021 and NSE/INSP/48655 dated**	**Penalty Levied**

		June 18, 2021	
		LO-1	
1.	The Noticee has not collected adequate margin from its clients in the form of cash, cash equivalent or Group I equity shares, with appropriate haircut in 50 instances amounting to Rs.103.62	5% of falsely reported margin amount capped at Rs.15,00,000	Rs. 15,00,000/-
2.	The Noticee reported incorrect margin collection from the clients to the Exchange in 1 instance amounting to Rs. 2.34 lakhs.	10% of falsely reported margin amount	Rs.23,400/-
3.	The Noticee submitted incorrect data towards weekly monitoring of clients' funds under the Enhanced Supervision of Stockbrokers in 2 areas involving Rs. 0.02 Crore and Rs.338.48 crores as on December 31, 2021	Warning to Rs.1,00,000/-	Rs.1,00,000/-
4.	The Noticee uploaded incorrect data towards weekly holding statement in 3 instances amounting to Rs. 8.36 lakhs.	Rs.1,00,000/-	Warning
5.	The Noticee reported incorrect client ledger balance in case of 2 clients amounting to Rs. 2.89 lakhs towards weekly client level cash and cash equivalent balances	Rs.1,00,000/-	Warning
6.	The Noticee has not maintained a daily reconciliation statement indicating the details of the said transfer of funds between accounts in case of 803 instances.	Rs.25,000/-	Rs.25,000/-

7.	The Noticee has not maintained the bank books correctly.	Rs.25,000/- per book	Rs. 25,000/-
8.	Mismatches in the email ids and mobile numbers mapped to the clients as per the Noticeef's back-office records and those uploaded on the UCC database of the Exchange	Rs.1,000/- per client	Rs.5,000/-
9.	The Noticee has delayed the settlement of clients' funds in case of 2 out of total 100 instances verified amounting to Rs. 59,706/-, thereby constituting 2% of the total samples verified	Up to 50% of the instances verified – Warning / Advise	Warning
10.	The Noticee submitted incorrect net worth to the Exchange for the half year ended on September 30, 2021	No Prescribed Penalty	Warning
11.	The Noticee has not reported closure of their 5 demat accounts to the Exchange within one week of the closure	Rs.5,000/- + Warning + Direction to report such details to the Exchange	Rs.5,000/- + Warning + Direction to report such details to the Exchange
		SCN	
12.	The Noticee facilitated the financing of clients' transactions through a financier	Rs.5,00,000/-	Rs.5,00,000/- + directions to stop financing of client transactions through financier with immediate effect
LO-2			
13.	The Noticee has engaged as a principal in a business other than securities involving personal financial liability involving Rs.905.35 crores and Rs.566.33 crores in MOFL and MOHFL respectively	Amount involved > Rs. 5 Crores : Penalty of Rs. 5 Lakhs + No new clients if funds given as loans / advances are not recovered within the time allotted	Rs.5,00,000/- + Direction as mentioned in Para 9.13.4 of this order.
	Total		**Rs. 26,83,400/-**

11. The Noticee is directed as under: -

a. To pay a monetary penalty of Rs. 26,83,400/- (Rupees Twenty-Six Lakhs Eighty Three Thousand and Four Hundred only).

b. To note the non-monetary penalties mentioned above and ensure non-recurrence of the observed violations.

Sd/-	Sd/-	Sd/-
Mona Bhide (Chairperson)	K Narasimha Murthy (Committee Member)	S Ravindran (Committee Member)

Sd/-	Sd/-
Ranganayakulu Jagarlamudi (Committee Member)	Ashishkumar Chauhan (Committee Member)

Date: September 26, 2023