Before the

MEMBER AND CORE SETTLEMENT GUARANTEE FUND COMMITTEE

Of

NSE Clearing Limited

Exchange Plaza, Bandra Kurla Complex, Bandra East, Mumbai – 400051

In the matter of regular inspection of Clearing Member

M/s. Nuvama Clearing Services Limited

(Erstwhile M/s. Edelweiss Custodial Services Limited)

CORAM:

Mr. G S Hegde	-	Chairperson of the Committee
Mrs. Bhagyam Ramani	-	Committee Member
Mr. Jayant Haritsa	-	Committee Member
(through video conference)		
Mr. Golaka C Nath	-	Committee Member
Mr. Vikram Kothari (MD)	-	Committee Member

41st Meeting of the Committee held on December 6, 2022 at Exchange Plaza, Mumbai

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I. BACKGROUND

1.1 Nuvama Clearing Services Limited (erstwhile Edelweiss Custodial Services Limited (**"ECSL"** or **"the Noticee"**), having its registered office at Tower 3, Wing 'B', Kohinoor City Mall, Kohinoor City, Kirol Road, Kurla (West), Mumbai 400070, is registered as a Clearing Member, in the sub-category of Professional Clearing Member **("PCM")** with NSE Clearing Limited ("**NCL**") (SEBI Registration No. INZ000177437).

1.2 NCL conducted regular inspection of the Noticee in F&O and CD segment for the period January 1, 2018 to June 30, 2020.

1.3 NCL vide its letter dated June 11, 2021, sent an initial letter of observation and final letter of observation was sent on July 5, 2021 to the Noticee to which the Noticee replied vide its letter dated July 22, 2021 with a delay of ten days.

1.4 NCL issued a Show Cause Notice ("**SCN**") dated August 24, 2021, to the Noticee for the following alleged violations: -

a) 40 instances of failure to collect margin from 7 trading members in violation of Regulation 4.5.1 of the NCL Regulations (F&O segment) ("**NCL Regulations**")

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b) 17 instances of non-adherence to prudent risk management policies in violation of Clause 1 and Clause 2 read with Clause 3(1)(b) and Clause 3(1)(c) of Chapter V of the NCL Rules,

c) Failure to close one beneficiary demat account within the time frame as required by the Exchange's circulars bearing No.: NSE/INSP/41359 dated June 20, 2019, bearing No. NSE/INSP/42000 dated August 29, 2019, bearing No.: NSE/INSP/42052 dated September 4, 2019, and NCL's circulars bearing No. : NCL/CMPL/41442 dated June 28, 2019, and bearing No.: NCL/CMPL/42015 dated August 30, 2019

1.5 The Noticee furnished its reply to the SCN vide its letter dated September 8, 2021 and denied the allegations in the SCN.

1.6 The Noticee was given an opportunity of personal hearing before the 34th meeting of the Member And Core Settlement Guarantee Fund Committee ("**MCSGFC"** or "**the Committee"**) held on October 6, 2021 and the Noticee vide its email dated October 6, 2021, submitted an additional compilation of documents to be referred during the personal hearing on October 6, 2021. The following members were present on behalf of the Noticee:-

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Sr. No.	Name of the Representative	Particulars
1	Mr. Prashant Mody	Head-Legal & Compliance- Edelweiss Custodial Services Ltd.
2	Mr. Atul Bapna	EVP- Edelweiss Custodial Services Ltd.
3	Mr. Gaurav Joshi	Senior Counsel
4	Mr. Sameer Pandit	Legal Advisor- Wadia Gandhi
5	Ms. Krina Gandhi	Legal Advisor- Wadia Gandhi

1.7 After hearing the matter at length, the Committee, based on the request of the advocates of the Noticee, granted them time to furnish further written submissions, if any, by October 13, 2021. The Noticee filed its additional written submissions dated October 13, 2021. The replies of the Noticee vide its letters dated September 8, 2021, October 6, 2021 and October 13, 2021 are herein after collectively referred to as "**Initial Submissions".**

1.8 The matter was considered again in the 36th meeting of the MCSGFC held on January 19, 2022, and the Committee directed that the Noticee be called upon to furnish certain additional information. Consequently, NCL vide its letter dated March 17, 2022, sought additional/further information/clarifications from the Noticee and called upon the Noticee to submit its reply on or before March 31, 2022.

1.9 By its email dated March 31, 2022 to NCL, the Noticee contended that it was in the process of obtaining legal advice in respect of the additional

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information/clarifications sought vide NCL's letter dated March 17, 2022 and requested for additional 10 days' time to respond to the NCL letter in detail. In response to the above email of the Noticee, NCL gave additional time to the Noticee and required the Noticee to submit its reply on or before April 10, 2022, but the Noticee failed to file its response on or before April 10, 2022, also.

1.10 By letters dated March 31, 2022 and April 19, 2022, the Noticee's advocates, M/s Wadia Ghandy & Co. requested NCL to furnish the Noticee/its advocates, a copy of the directions/advice of MCSGFC based on which the NCL letter dated March 17, 2022 was issued to the Noticee by NCL. NCL vide its letter dated April 20, 2022 in reply, stated that the information sought by the Noticee through its advocates are the internal notings of the MCSGFC and hence NCL is unable to provide the same to the Noticee.

1.11 The matter was again considered at the 37th meeting of the MCSGFC held on April 22, 2022, wherein the Committee was updated that vide NCL's letter dated March 17, 2022, the Noticee was called upon to furnish the required information and extension of time was granted as requested by the Noticee, but no response was filed by the Noticee. The Committee was informed that NCL vide its letter dated April 20, 2022, had once again directed the Noticee to furnish the information on or before April 27, 2022, failing which the matter would be viewed seriously and appropriate action as deemed fit may be taken.

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1.12 The Noticee filed its submissions vide its letter dated April 27, 2022 and, inter alia, contended that :-

> *"*At the outset, we state that Your Letter purports to have been issued as per the advice of the MCSGFC. Accordingly, vide our Advocate's letter dated March 31, 2022, and email dated April 19, 2022, we had sought for a copy of the said directions/advice of the MCSGFC on the basis of which you claim Your Letter was issued. However, vide your letter dated April 20, 2022, you refused to provide the said information. This lack of transparency about directions of the MCSGFC suggests a lack of impartiality which is the bedrock of quasi-judicial proceedings conducted by committees of exchanges and clearing corporations.
>
> Additionally, ECSL submits that much of the information sought goes far beyond the original SCN and is in fact in the nature of fresh inspection/audit after issuance of the SCN and completion of the oral hearing in the matter. Such attempts to bring in matters that travel beyond the scope of the SCN violates basic rules of natural justice and fair play.
>
> Without prejudice to the aforesaid and even though we have no obligation to comply with such directions, under protest we are furnishing our responses to

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such of the queries that may have even a tangential connection to the SCN to avoid the action as threated by you in your letter dated April 20, 2022.*"*

The Noticee in its aforesaid reply had inter alia alleged that much of the information sought by NCL goes far beyond the original SCN and had even alleged that the same was a 'fishing inquiry' and amounted to a fresh inspection/audit after issuance of the SCN and completion of the oral hearing in the matter.

1.13 Vide its letter dated September 22, 2022, NCL once again requested the Noticee to provide information/clarification relating to two observations consequent to the regular inspection as mentioned in the SCN, on or before September 29, 2022.

1.14 The Noticee vide its email dated September 30, 2022, requested to grant 15 days additional time to submit its replies. NCL acceded to the Noticee's said request and vide its email dated September 30, 2022, NCL requested the Noticee to submit its replies to NCL on or before October 14, 2022 and stated that matter would be placed before the Committee for consideration in the last week of October 2022.

1.15 The Noticee provided its submissions vide a letter dated October 14, 2022.

1.16 In view of the contention of the Noticee that much of the information sought by NCL goes far beyond the original SCN, in the interest of providing the Noticee

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adequate opportunity to defend itself, NCL issued a Supplementary Show Cause Notice ("**SSCN**") dated October 25, 2022, calling upon the Noticee to show cause as to why appropriate disciplinary action in terms of Rule 1 and/or Rule 2 of Chapter V of the NCL (F&O) Rules should not be taken against the Noticee for inter alia the following violations :-

a) Incorrect reporting under MG 12 in respect of Trading Member's proprietary margins obligations in violation of Item 14 of NCL circular download reference No. 34657 dated April 17, 2017 ("**NCL 2017 Circular**") and SEBI circular no. CIR/DNPD/7/2011 dated August 10, 2011 ("**SEBI 2011 Circular**")

b) Non-adherence to prudent risk management policies, in violation of Clause 1 and Clause 2 read with Clause 3(1)(b) and Clause 3(1)(c) of Chapter V of the NCL Rules ("**NCL Rules**")

The Noticee was also informed that an opportunity of personal hearing before the MCSGFC would be given on November 1, 2022.

1.17 The Noticee vide its email dated October 28, 2022 stated that it is in the process of considering the SSCN and preparing a response and requested NCL to give 2 weeks' time to file its response to the SSCN and also requested to fix a personal hearing thereafter. NCL vide its email dated October 28, 2022 in response, informed the

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Noticee to remain present before the MCSGFC on November 1, 2022 and make its request to the MCSGFC. The Noticee's representatives attended the personal hearing on November 1, 2022 and on various grounds they requested for extension of time to any date subsequent to November 10, 2022 for the filing of their reply to the SSCN. The member was represented by the following officials: -

Sr. No.	**Name of the Representative**	**Particulars**
1	Mr. Nikhil Johari	Designated Director
2	Mr. Atul Bapna	Head of Compliance
3	Mr. Bhoumik Mehta	Compliance Officer
4	Mr. Udit Sureka	Designated Director

The Committee acceded to the request and directed the Noticee to file its reply to the SSCN on or before November 15, 2022.

1.18 The Noticee then filed its reply to the SSCN vide its letter dated November 15, 2022 ("**Reply to SSCN**").

1.19 NCL vide its emails dated November 22, 2022 and November 24, 2022 informed the Noticee that it would be granted a personal hearing by the Committee on November 29, 2022 at 3pm. However, the Noticee's advocates vide their email dated November 28, 2022 sought an adjournment of the hearing for the convenience of its advocates and the same was once again acceded to and by an email dated November

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28, 2022, the Noticee was intimated that it would be given a personal hearing before the Committee on December 6, 2022.

1.20 As requested by the Noticee, the hearing was held through video conferencing on December 6, 2022. The following officials and lawyers of the Noticee were present during the hearing before the Committee via video conference:

Sr. No.	**Names of officials**
1	Mr. Udit Sureka- Designated Director
2	Mr. Prashant Mody- Head Legal and Compliance
3	Mr. Atul Bapna - EVP & Head of Compliance
4	Mr. Gaurav Joshi – Senior Counsel
5	Mr. Sameer Pandit – Partner, Wadia Ghandy & Co
6	Ms. Krina Gandhi – Senior Associate, Wadia Ghandy & Co
7	Mr. Anmol Menon – Associate, Wadia Ghandy & Co

1.21 At the personal hearing held on December 6, 2022, the Senior Counsel representing the Noticee made his oral submissions on behalf of the Noticee and requested to give time till December 13, 2022 to file additional written submissions. The Committee

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acceded to the request and gave time till December 13, 2022 to the Noticee to file its written submissions. Accordingly, Noticee filed its written submissions dated December 13, 2022 ("**Reply to SSCN**").

1.22 The Committee meticulously considered the oral submissions made on behalf of the Noticee during the personal hearing, the various replies and written submissions made by the Noticee, for arriving at a conclusion on the alleged violations.

II. THE FIRST VIOLATION AS ALLEGED IN THE SCN and SSCN

The details of the alleged violation as stated in the SCN and SSCN, Noticee's submissions to SCN and SSCN and the findings of the Committee are discussed hereinbelow: -

1. **The first violation alleged in the SCN is that it was observed that there are 40 instances wherein the Noticee failed to collect margin from 7 trading members in violation of Regulation 4.5.1 of the NCL Regulations.**

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2. The Noticee's Initial Submissions and the findings of the Committee are summarized herein below: -

2.1 Noticee has stated that the SCN fails to specify how Noticee has purportedly violated Regulation 4.5.1 of the NCL Regulations. Regulation 4.5.1 provides as follows: -

> "The F&O Clearing Members shall demand from its constituents the margin monies which the clearing member has to provide under these Regulations in respect of dealings done by the F&O Clearing Members for such constituents."

Regulation 4.5.1 requires a CM to "demand" margin monies from its constituents. Moreover, Noticee's primary obligation is to place sufficient margin and ensure that it honors its settlement obligations. Noticee has robust risk management system which tracks all TM level risk through integrated system to curtail the Noticee's risk at appropriate levels. Noticee has ensured that it was always compliant with this obligation and has not fallen short of its margin obligations towards NCL during the relevant period.

The Noticee has an obligation to only "demand" margin monies from its constituents. There is no time limit prescribed in Regulation 4.5.1 within which actual collection of margin has to be completed. This is also in line with the model CM-Agreement which too does not contain a statutory or regulatory mandate of

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the time within which a margin shortfall has to be recovered from the TM. This is the only reasonable interpretation of the Regulation and the structure of the market, as a CM cannot be blamed for the failure of a TM to replenish his margin shortfall. In case a TM does not replenish his margin shortfall after the CM has raised a demand, the CM takes action as per its risk policy. There is no allegation against the Noticee in the SCN that it failed to "demand" margin from its constituents.

With regard to the Noticee's submissions above, the Committee notes that the requirement to demand margins from its constituents under Regulation 4.5.1 includes collection and retention of the margins collected as long as the outstanding position remains, and margin obligations continue. The Noticee's purported interpretation is untenable and would lead to the absurd position that margins have to be demanded but need not be collected or retained by the CM. Such an interpretation as espoused by the Noticee, would defeat the entire purpose of the stipulation for margins and would undermine the risk management system. It may also be noted that the actual margin collected from the constituents are required to be reported to the Clearing Corporations on a daily basis. The SEBI 2011 circular has prescribed penal provisions for short collection/non collection of margins. No Clearing Member can be permitted to state that they have demanded the margin but need not collect and retain the margin under Regulation

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4.5.1. Margins must be collected for all open positions and must be retained and updated as long as the position is open and outstanding.

The Committee therefore observes that it is abundantly clear from Regulation 4.5.1 read with SEBI 2011 Circular that CM has to demand and collect the margins and retain margin till the position remains open. The contention of the Noticee that it had demanded the margins from the clients and satisfied the requirement of Regulation 4.5.1 deserves to be rejected as being frivolous, fallacious and as a mere after thought to try and justify its erroneous conduct.

2.2 Noticee submitted that Clearing members (CM) are required to enter into a CM-TM Agreement based on the model form prescribed by NCL and NSE with each TM. Clause 5(4) of the Model CM-TM Agreement provides as follows: -

> "The Trading Member shall pay to the Clearing Member margins of such amounts as may be prescribed by NSCCL from time to time including additional margins, if any, or such higher amount of margins as may be mutually agreed with the Clearing Member. The margins shall be deposited by the Trading Member within such time and in such form as may be specified by the Clearing Member."

With regard to the Noticee's submission above, the Committee observes that the Noticee has referred to the clause 5(4) of the model CM-TM agreement emphasizing that the trading member and clearing member may mutually agree on amount of margin, time of payment as well as form of payment of such margin. However, as per the same model agreement, the clearing members are required

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to ensure that the margin so collected shall not be less than the amount stipulated by NCL. The relevant extract of clause 2(5) is as follows: -

> *'(5) Clearing Member shall be entitled to collect from Trading Member margin(s) of such amounts of such kinds, as he may deem necessary, which at any point of time shall not be less than the amount stipulated by NSCCL from time to time. The Clearing Member shall have authority to collect such additional margin(s) as the Clearing Member may deem necessary or as per the requirement of NSCCL.'*

This clause also entitles the clearing member to demand additional margin in case the collaterals already collected from the constituents are insufficient to cover market fluctuations/MTM loss.

2.3 Out of the 40 instances identified in the SCN, 31 instances pertain to Anugrah Stock & Broking Pvt. Ltd. **("Anugrah").** Instances relating to Anugrah were already the subject matter of a Show Cause Notice dated September 19, 2020 issued by NCL and the order dated October 20, 2020 passed by the MCSGFC. The said order of the MCSGFC was challenged by the Noticee before the Hon'ble Securities Appellate Tribunal ("Hon'ble SAT") in Appeal (L) No. 441 of 2020. The said order of NCL was stayed by the Hon'ble SAT vide its order dated November 5, 2020. As such the instances relating to Anugrah are already the subject matter of ongoing legal proceedings. Since the matter is sub-judice before the Hon'ble SAT, Noticee requested NCL to exclude this observation from the purview of the present SCN.

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With regard to the Noticee's submissions above, the Committee observed that the Noticee has provided the data with respect to Anugrah under protest. However, the Committee notes that the issue in the present proceedings is totally different from the issue in the said previous proceedings which is pending before the Hon'ble Securities Appellate Tribunal in Appeal 441 of 2020, which relates to the wrongful sale of Anugrah's clients shares by the Noticee and the same does not relate to the Noticee's failure to collect margin from TMs in accordance with Regulation 4.5.1 of NCL Regulations (F&O segment) and the wrong reporting of margins, which is the issue in the present proceedings. Accordingly, the Committee is not precluded from passing an order pursuant to the SCN and SSCN in respect of the aforesaid allegation of failure to collect upfront margin from its trading members and for wrong reporting of margins, including in respect of Anugrah.

2.4 For the remaining 9 instances which pertain to 6 Trading Members, Noticee has submitted that it has a well-established and inviolable system for setting limits commensurate with the margin placed by a TM. As an invariable feature of the system, Noticee provides position limits to TMs based on the margins placed by the TMs. Accordingly, required upfront margin was collected from each concerned TM when position limits were set for such TM. As such, Noticee had collected required initial margin and was fully compliant with Regulation 4.5.1 at the time

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the concerned TMs were offered position limits. There is no allegation in the SCN that Noticee has granted position limits to any TM beyond the margin that was collected.

With regard to the Noticee's submission above, the Committee notes that this submission of the Noticee is also not tenable since the Clearing Members are required to ensure that the upfront margins collected shall be maintained at all points in time as long as the positions are open, since the liability is a continuing liability.

2.5 Instances identified in the SCN do not relate to failure of the Noticee to collect upfront margin from the TM but relate to shortfall in margin that arose on account of MTM losses suffered by such TMs during trading or on account of fluctuation of securities valuation due to market volatility. Given the inherent volatility of the F&O segment, there are inevitably certain instances when the MTM losses of a particular TM increase on account of market fluctuations. As a result, the upfront margin placed by the TM with the CM may not be sufficient to cover such MTM losses. Such MTM losses are an inherent feature of the F&O segment and are entirely outside the control of the CM. It is therefore submitted that the mere fact that a particular TM has suffered an MTM loss which results in erosion of margin can never amount to a violation of Regulation of 4.5.1 by the CM.

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With regard to the Noticee's submission above, the Committee notes that the SCN pertains to non-collection of upfront margins, and the Noticee's submissions pertaining to MTM losses are not relevant to the alleged violations.

2.6 The Noticee has a robust and well-defined internal risk policy to deal with cases of margin shortfall. In case a TM suffers MTM losses that outstrip the margin placed by such TM, the Noticee immediately calls upon the TM to regularize its account for making good its margin obligations. The Noticee's team reaches out to the concerned TM and informs the TM of the shortfall in its account. The Noticee on ongoing basis engages with TMs and ensures that the required margins are collected from TMs. The TM is also asked to make good the shortfall and regularize its account.

With regard to the Noticee's submission above, the Committee noted the contention of the Noticee that a mere demand for margin is sufficient and need not be followed up by the actual receipt of the margin has to be and is rejected outright by the Committee in view of Regulation 4.5.1 and SEBI 2011 Circular referred to above.

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2.7 The TMs are further informed of the shortfall in their account in the form of a Daily Activity Statement ("**DAS**") that is sent to them by the Noticee at the end of the trading day. The DAS specifically sets out the margin obligation that the TM is liable to make good. After being intimated of the margin shortfall, the account is regularized in one of the following ways: (i) TM brings in additional collateral; (ii) Value of the existing collateral rises in subsequent days; (iii) Positions are reduced by TM which leads to reduction in margin requirement. In the event the shortfall persists, and the TM does not regularize its account despite reminders, then the Noticee takes appropriate steps in accordance with its risk policy which includes placing the TM in Risk Reduction Mode ("**RRM**") i.e. preventing the TM from taking any fresh positions, initiating liquidation of collateral, etc. In case the shortfall in the proprietary trading account of a TM persists, then the Noticee immediately reports to NCL.

Necessary steps were taken in each of the 9 instances identified in the SCN to ensure that the accounts were regularized by the TMs by meeting their margin requirements. As per the Noticee's policy, in each of the instances where the TM suffered a margin shortfall, the Noticee sent an email to the concerned TM with the Daily Activity Statement, Daily Margin and Limit Summary and Consolidated Report across segments. The documents set out the margin obligation shortfall of such TMs and required the TM to make good the margin obligation. Upon

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issuance of the aforesaid email to the concerned TMs, Noticee has complied with its obligation under Regulation 4.5.1 to demand margin from its constituents.

The Noticee has also taken proactive steps to cause the concerned TMs to make good their margin obligations. The Noticee has provided the details showing how the accounts of the TM's were allegedly regularized in each of the 9 instances identified in the SCN.

Sr. No.	Date of shortfall as per SCN	TM Name	Date of regularization	Mode of regularizing the account
1.	23.01.2018	V-Rise Securities Pvt Ltd	26.01.2018	Positions were reduced by TM which led to reduction in margin requirement by Rs.32.94 crore
2.	28.08.2018	Relitrade Stock Broking	30.08.2018	Value of collateral increased by Rs.2.11 crore and positions were reduced by TM which led to reduction in margin requirement by Rs.17.26 crore
3.	28.08.2018	BMA Wealth Creators Ltd.	29.08.2018	Positions were reduced by TM which led to reduction in margin requirement by Rs.2.55 crore
4.	11.10.2018	Edelweiss Securities Ltd.	12.10.2018	Positions were reduced by TM which led to reduction in margin requirement by Rs.1.9 crore
5.	19.12.2018	Relitrade Stock Broking	20.12.2018	Positions were reduced by TM which led to reduction in margin requirement by Rs.14.2 crore
6.	26.03.2019	Global worth Securities Limited	27.03.2019	Value of collateral increased by Rs.17.02 crore
7.	23.09.2019	Global worth Securities Limited	25.09.2019	Value of collateral increased by Rs.23.1 crore
8.	23.10.2019	Global worth Securities Limited	24.10.2019	Value of collateral increased by Rs.1.02 crore andPositions were reduced by TM which led to reduction in margin requirement by Rs.60.54 crore

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As regards the shortfall in the account of Indianivesh Shares and Securities Private Limited on April24, 2019, the said TM was onboarded with the Noticee on April 24, 2019. Since it was under transition mode, the account of the said TM had a shortfall on the said date of onboarding as the collateral by way of FDR/BG was being transferred from the previous CM to the Noticee. Upon receipt of the same, the collateral increased by Rs. 119.93 crore and the account was regularized on April 26, 2019.

Therefore, in each of the identified 9 instances, the Noticee took appropriate action to regularize the accounts of the TMs and ensured due compliance with Regulation 4.5.1. Moreover, Noticee has fulfilled all its margin obligations towards NCL on a regular basis and has ensured that sufficient collateral is available with NCL.

With regard to the Noticee's submission above, the Committee noted that the Noticee has submitted that it had regularized the shortfalls pertaining to certain trading members within the time gap of 1 to 3 days. However, the contention of the Noticee is not acceptable since the shortfall pertains to upfront/initial margins which cannot be "regularized" subsequently as it has to be collected on an

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upfront basis, i.e. before the order is placed. The Committee therefore noted that the Noticee failed to collect adequate initial / upfront margins.

2.8 All the other provisions of Regulation 4 (other than Regulation 4.5) deal with a CM's margin obligation towards NCL and do not apply to margin to be placed by constituents/TM with a CM. Thus, Noticee's primary obligation is to place sufficient margin with NCL and ensure that it honors its settlement obligations. In this regard it is necessary to appreciate that there is no allegation or reference in the SCN about failure to demand or collect "Upfront Margin" or granting position limits to TMs beyond the value of collateral placed by them. The Noticee has also submitted that it has never fallen short of its margin obligations towards NCL.

With regard to the Noticee's submission above, the Committee notes that the Noticee was duty bound to collect the NCL stipulated margins from its TMs and report daily to NCL the amount of margins collected from each TM, and any short collection of margins would expose the Noticee to penalties. Placing sufficient margin with NCL is not a defense for failure to collect sufficient margin from TM.

2.9 During the hearing attempts were made to go beyond the scope of the SCN in violation of established principles of quasi-judicial process and natural justice. For the purposes of the hearing, NCL had relied upon only the SCN, and the two Exhibits annexed to the SCN. NCL did not presentany further documents prior to

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or even during the hearing. When Noticee submitted that Regulation 4.5.1 only requires the CM to "demand" margin and does not prescribe any timelines, officials of NCL attempted to make reference to certain other unnamed or unspecified circulars/provisions. Reference was also sought to be made by the officials of NCL to purported discussions/clarifications given during the inspection by the inspection team. This was also referred to by the KMP of NCL who is part of the MCSGFC. During the hearing a completely new case was raised, and it was suggested that the allegation in the SCN should be read and interpreted to mean that it relates to Noticee's failure to collect "Upfront Margin" and not towards margin for losses / MTM losses suffered by the TM. The Noticee objected to this and submitted that new allegations not forming part of the SCN cannot be raised for the first time in the hearing. It was also pointed out that the SCN was required to be self-contained and members of the MCSGFC were required to adopt a neutral and unbiased stand without relying upon any purported "conversations" or "understandings" that allegedly took place during the inspection process which find no reference in the SCN. The proceedings could not go beyond the scope of the SCN and the same would be in violation of the principles of natural justice and fair play.

In this regard, it is necessary to appreciate that there is no allegation or reference in the SCN about failure to demand or collect "Upfront Margin" or granting position limits to TMs beyond the value of collateral placed by them. A plain

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reading of the aforesaid makes it clear that no mention whatsoever has been made to "Upfront Margin". Similarly, Exhibit – 1, which refers to the specific instances of purported default also does not refer to "Upfront Margin". It only refers to the following three parameters: (i) FO + CD Collateral (Rs. In Crs); (ii) FO + CD Margin (Rs. In Crs.); and (iii) Shortfall (Rs. In Crs.). This cannot possibly be interpreted to mean that the SCN relates to a purported failure to collect "Upfront Margin". In fact, even Regulation 4.5.1 is not specific to "Upfront Margin" and only refers to the CM's obligation to demand "margin" in general. On the other hand, the fact that the SCN does in fact contemplate reference to MTM losses is apparent from para 4 (ii) of the SCN which expressly refers to MTM losses while dealing with 17 instances relating to Anugrah. A comparison of Exhibits 1 and 2 to the SCN makes it clear that these 17 instances are also for the same dates that are referrable to para 4 (i) of the SCN.

The SCN only makes reference to Regulation 4.5.1 and not to any other legal provision. As such, the instant proceedings cannot be expanded to cover any other purported allegations regarding violation of other unspecified circulars or provisions as it would amount to condemning the Noticee for matters that go beyond the SCN, which is impermissible in law.

With regard to the Noticee's submission above, the Committee notes that Exhibit 1 of the SCN contained details of instances of margin shortfall, excluding MTM.

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Further, data sheet giving break up of Exhibit 1 to the SCN was shared with the Noticee vide the NCL letter dated March 17, 2022, giving details of upfront margin, excluding MTM. The same was sourced from the data contained in the MG18 files, which are downloaded daily to the Noticee. Therefore, the Noticee was well aware that the shortfall pertains to upfront Margins, and not any subsequent MTM losses.

3. *The Committee noted that though the violation alleged in the SCN did not use the words 'upfront margin', it was clear from the correspondence between NCL and the Noticee (during the period from March 17, 2022 to September 22, 2022) that the violation alleged was with respect to Noticee's failure to collect upfront margins. However, for the sake of good order and to provide the Noticee a full-fledged opportunity to defend itself against the allegation of failure to collect upfront margin, it was decided that a SSCN be issued to the Noticee.*

4. NCL then issued the SSCN for the violation of Item 14 of NCL circular download reference no. 34657 dated April 17, 2017 and SEBI circular no. CIR/DNPD/7/2011 dated August 10, 2011, for incorrect reporting under MG 12 for Trading Member's proprietary margins obligations. The violation alleged in the SCN was subsumed in the SSCN as follows: -

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"**Incorrect reporting under MG 12 for Trading Member's proprietary margins obligations.**

Non-adherence to Item 14 of NCL circular download reference no. 34657 dated April 17, 2017 and SEBI circular no. CIR/DNPD/7/2011 dated August 10, 2011.

a) There were 40 instances wherein the Noticee had failed to collect upfront margin from 7 trading members i.e., short collection of upfront margin, as per Exhibit 1 of SCN dated August 24, 2021 which was also elaborated in the Exhibit 1 of NCL letter dated March 17, 2022, in accordance with Regulation 4.5.1 of NCL Regulations (F&O segment)"

b) Although vide the NCL's said letters dated March 17, 2022 and September 22, 2022, further information was sought from the Noticee, the Noticee failed to clarify or submit any supporting documents with respect to the due diligence carried out while reporting under MG12 - i.e. - collection and reporting of upfront margin for TM's proprietary obligations in case of six instances noted in Annexure A of NCL's September 22, 2022 letter. The Noticee vide its reply dated October 14, 2022 submitted that *"...*the MG12 reporting was done considering the Proprietary Margin v/s total collaterals of TM available *..."* with the Noticee.

c) While reporting under MG12 the Noticee is required to separately and specifically identify margins/collaterals collected from the TMs only for TM's proprietary trades. Upon inquiry, the Noticee expressly represented that for

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MG12 reporting it had considered the total collaterals available, being both proprietary and client collateral and had failed to provide the details/particulars of the break-up between the client collateral and TM proprietary collateral despite repeated request for the same by NCL.

d) It would therefore appear that the Noticee is avoiding full disclosure to conceal the fact that to its knowledge, there was a shortfall of TM's proprietary margin and that the reporting done in MG12 was incorrect and there was a shortfall of collection of TM's proprietary margin.

e) The Noticee failed to carry out due diligence while doing the MG12 reporting, and incorrectly reported the proprietary collaterals for six instances as given in Exhibit A of the NCL's September 22, 2022 letter.

f) The Noticee was also informed that false reporting of proprietary margin collection from trading members is in violation of SEBI circular no. CIR/DNPD/7/2011 dated August 10, 2011 and would attract penalty as prescribed in the circular and also as prescribed in SEBI circular no. CIR/HO/MIRSD/ DOP/CIR/P/2019/88 dated August 1, 2019 read with NCL circular no. 42946 dated December 19, 2019.

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5. The Notice's Reply to the SSCN and the findings of the Committee are summarized herein below**:** -

5.1 No order was passed on the SCN. Since the SSCN was issued after considering the submissions previously made by Noticee in respect of the allegations in the SCN and the SSCN contained the final set of violations which the Noticee was required to answer, the submissions made by Noticee at the hearing held on December 6, 2022 were restricted to the allegations in the SSCN since all other allegations raised in the previous communications / SCN stand satisfactorily explained. Should any order be passed on the SCN at this stage, Noticee reserves its rights to object to the jurisdiction, authority and power to pass an order on the SCN.

With regard to the Noticee's submission above, the Committee noted that the violation alleged in the SCN have been appropriately dealt with in this order for the sake of clarity and by way of background leading to the issue of SSCN. It is not correct to say that the allegations in the SCN have been explained satisfactorily. As the violations alleged in the SCN are duly subsumed into SSCN the Committee passes this order on the violations as alleged in the SSCN.

5.2 The Noticee denies that there has been any incorrect reporting of margin in respect of the Trading Member's proprietary obligations or any non-disclosure or concealment of facts. As per the NCL 2017 Circular, a CM is required to provide

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details of margins for a proprietary account of the TM by way of the MG-12 file. Thus, the MG-12 file is only in respect of the proprietary obligations of a TM. There is no provision in the MG-12 file to report margin obligation of the end-clients of TM. Further, there is no provision in either the NCL 2017 Circular or the SEBI 2011 Circular for providing details/particulars of the break-up between the client collateral and TM proprietary collateral as wrongly alleged in the Supplementary SCN. In fact, the NCL 2017 Circular provides a format of the MG-12 file. The Noticee has correctly reported the proprietary margin in accordance with the said format. The Supplementary SCN fails to identify which provision in the aforesaid circulars require a break-up of proprietary and client margin requirements and respective available collateral to be furnished vide the Form MG12. The margin obligation and available collateral of the end-clients are required to be reported by the TMs in the MG-13 file.

Exhibit A to SSCN is completely incorrect as the same considers the consolidated margin obligation for proprietary and client positions of the TM for reporting under MG-12. Considering that the MG-12 file is supposed to contain only the proprietary margin obligations of a TM, Noticee has tabulated the proprietary margin obligation for the 6 instances mentioned at Exhibit A of the SCN and the collateral available with Noticee as follows: -

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Date	TM Code	TM Name	Total Collaterals for FO + CD (Rs. In Crs)	Total Upfront Margin Obligation as per SSCN (FO +CD) (Rs. In Crs.)	Total Proprietary Upfront Margin Obligation for FO +CD (Rs. In Crs.)	Shortfall (Rs. In Crs.)
(A)	(B)	(C)	(D)	(E)	(F)	(G)
23-Jan-18	12889	V-Rise Securities Pvt Ltd	31.91	32.94	24.67	No shortfall
28-Aug-18	14905	Relitrade Stock Broking	65.71	66.93	31.2	No shortfall
19-Dec-18	14905	Relitrade Stock Broking	38.05	38.76	19.08	No shortfall
26-Mar-19	13994	Globalworth Securities Limited	139.07	146.77	69.39	No shortfall
23-Sep-19	13994	Globalworth Securities Limited	212.28	223.05	95.96	No shortfall
23-Oct-19	13994	Globalworth Securities Limited	248.03	256.76	104.51	No shortfall

Column E above sets out the margin requirement as calculated in the SSCN. This is incorrect for the purposes of MG-12. On the contrary, column F above correctly sets out the margin requirement for proprietary positions which is the subject matter of MG-12. As evident from the above, the Noticee had collected sufficient upfront collateral to cover the proprietary margin obligations on all 6 instances and there was no shortfall in the collection of TM proprietary margin. Therefore, the reporting done by the Noticee in MG-12 was correct and the Noticee has not violated or failed to adhere to the provisions of the SEBI circular

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no. CIR/DNPD/7/2011 dated August 10, 2011 or SEBI circular no. CIR/HO/MIRSD/ DOP/CIR/P/2019/88 dated August 1, 2019 or the NCL circular no. 42946 dated December 19, 2019. Accordingly, no penalty is attracted under the aforesaid circulars for false reporting of margin collection by the Noticee from the Trading Members.

The Noticee had collected sufficient upfront collateral to cover the proprietary margin obligations of all 6 instances and there was no shortfall in the collection of TM proprietary margin or any incorrect reporting of margin. It is also pertinent to note that in some of the cases the cash collateral alone was sufficient to meet the margin obligation of the TM.

The SSCN appears to have proceeded on a complete misconstruction of the Noticee's letter dated October 14, 2022 and has wrongly assumed that the words "Total Collaterals of TM" mean consolidated collateral across proprietary and client positions. Total collateral quite obviously refers to the aggregate of all forms of collateral given by the TM that was allocated towards his proprietary positions and cannot possibly refer to consolidated collateral across proprietary and client positions. In any case, the MG-12 data furnished by Noticee speaks for itself and correctly reports the margin towards proprietary obligations. The same data also shows that there was no shortfall in margin for the instances referred to in Exhibit A to the Supplementary SCN.

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With regard to the Noticee's submission above, the Committee observed that after the end of trading hours on each trading day, the NCL issues the MG-12 file to each CM, inter-alia stipulating the proprietary trading margin requirement of each TM. The CM is required to fill in the quantum of proprietary margin collected from each TM and report / upload the same to the NCL. The Committee observes that in case of 40 instances as given in Exhibit 1 of the SCN, NCL sought clarification from the Noticee with respect to the due diligence carried out by the Noticee for ensuring correctness of the margin reporting and called upon the Noticee to submit supporting documents qua the collaterals reported to be collected and available, so as to demonstrate the correctness of the margin reporting. Subsequently, NCL vide its September 22, 2022 letter sought information about the collaterals collected from the TMs to demonstrate correctness of margin reporting for only 6 instances as set out in Annexure A to the SSCN, where the TM's had proprietary trade margin obligations. SEBI's circular dated May 2, 2018, inter alia stipulated as follows: -

'Margin Enforcement Requirement

3. With reference to SEBI circular CIR/DNPD/7/2011 dated August 10, 2011 captioned "Short-collection/Non-collection of client margins (Derivatives segments)", it is clarified that the 'margins', for both Equity Derivatives Segment and Currency Derivatives Segment, shall include margins as specified in Para 2 of this circular, mark to market settlements or any other

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margin as prescribed by the Exchange/Clearing Corporation to be collected by Clearing Members from their clients (i.e. Custodial Participants and Trading Members - for their proprietary positions) and by Trading Members from their clients.'

The Committee also notes that in case of four trading members viz. M/s. Anugrah Stock & Broking Private Limited, BMA Wealth Creators Limited, Edelweiss Securities Limited and Indianivesh Shares and Securities Private Limited, since there was no TM proprietary margin obligation on the dates given in the Exhibit 1 of the SCN, there was no MG12 reporting requirement by the Noticee.

The Committee notes that NCL vide Annexure A of its letter of September 22, 2022 provided the shortfall on the dates on which there were TM Proprietary margin obligations as given in the Exhibit 1 of the SCN dated August 24, 2021. The Noticee was required to comply with MG 12 reporting and therefore the Noticee was expected to submit true and correct details of proprietary collaterals received from the TMs towards their respective proprietary trading obligations. The Noticee was required to compare column F (Total Proprietary Upfront Margin Obligation for FO + CD (Rs. In Crs.) of its submission in its letter dated November 15, 2022 with actual proprietary collaterals received from the TMs towards their Proprietary trading obligations. However, the Noticee has apparently wrongly compared the same with total collaterals taken from the TMs, including TM's client collaterals.

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Thus, Noticee has incorrectly reported the margin collection for the 6 instances as given in Annexure A of the NCL September 22, 2022 letter. The Noticee was also informed that in absence of supporting data demonstrating that the requisite due diligence was carried out while reporting in the MG12, the Clearing Member is liable for the shortfall and wrong reporting.

The Committee further notes that the Noticee has admitted in its letter dated October 14, 2022 that for the 6 instances involving 3 TMs, the MG12 reporting was done considering the "Proprietary Margin v/s Total Collaterals of TM" available with Noticee.

The Committee also notes that the Noticee in its submissions instead of providing the details of Trading Member's proprietary collaterals, wrongly compared column D (total collaterals FO + CD which also includes the total collaterals of TM proprietary and end client of TM) with column F (which relates to only TM Propriety margin obligation) and thus wrongfully attempted to contend that there is no shortfall in margin collection.

The Committee also rejects the Noticee's belated afterthought and attempt to cover up and cause confusion vide its submission dated December 13, 2022 since the Noticee is obfuscating the fact that what it had reported in the MG12 as being the value of the TMs proprietary collateral / margin towards the TMs proprietary trade

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margin requirements, was not just the TMs proprietary collateral / margin, but also included the TMs clients collateral / margin, and that is why the Noticee is also refusing to furnish any documentary evidence to prove that the margin reported to be collected in the MG12 was only the TMs proprietary collateral / margin. In fact, the Noticee has not submitted any documentary evidence in this regard despite repeated requests for the same vide NCL's letters dated March 17, 2022 and September 22, 2022 .

However, the Noticee is now trying to attribute a different meaning to its admission contained in that letter. Since the Noticee has failed to produce any documentary proof to show that the margins reported in MG 12 were only proprietary margins and not total of proprietary and client margins, the Committee is satisfied that the explanation now offered is only an afterthought. Therefore, the Committee relies on the admission contained in Noticee's letter dated October 14, 2022 that the margins reported in MG 12 were total margins and not merely proprietary margin.

5.3 The Noticee submitted that it is also relevant to point out at this juncture that the allegation regarding non-provision of break-up between client collateral and TM proprietary collateral is not even relevant to the period under inspection which relates to January 1, 2018 to June 30, 2020. During this period, there was no provision enabling a CM to segregate the collaterals placed by a TM. Noticing this, the SEBI vide circular dated July 20, 2021 bearing no. SEBI/HO/MRD2_DCAP/CIR/2021/0598 and subsequently the NSE Clearing by

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its Circular dated March 17, 2022 bearing no. 030/2022 passed directions for allocation of collateral amongst the TM and clients. This requirement was not mandated during the period of inspection. Thus, the allegation that Noticee failed to specifically identify collateral collected from a TM towards the proprietary trades during the inspection period is completely misplaced.

With regard to the Noticee's submission above, the Committee observed that the contention of the Noticee is incorrect and cannot be accepted. The MG12 reporting requirement has been in existence since the NSCCL circular dated June 25, 2002 and the same did require the reporting of TMs proprietary collateral / margin for the TMs proprietary trades in the MG12 form; the reporting of the TMs clients' collateral / margin for the TMs clients' trades in the MG13 form. Therefore, the CM cannot claim that it was not required to segregate the proprietary and client collateral / margin. Further, the prescribed format of the CM - TM Agreement, inter alia stipulates that: -

> "…..
> *2 (5) . Clearing Member shall be entitled to collect from Trading Member margin(s) of such amounts of such kinds as he may deem necessary, which at any point of time shall not be less than the amount stipulated by the NSCCL from time to time. The Clearing Member shall have authority to collect such additional margin(s) as the Clearing Member may deem necessary or as per the requirement of NSCCL.*
>
> *(6) The Clearing Member shall be entitled to receive from the Trading Member such amounts as may be required to be paid towards daily mark to market settlement, final settlement or such other settlement as per the requirement of NSCCL at such intervals as may be mutually agreed upon by them.*

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8) The Clearing Member shall have authority to close out / liquidate the open positions of the Trading Member in accordance with the NSCCL Regulations, in case of non-payment of dues by the Trading Member towards margins, daily mark to market settlement, final settlement …….

……..”

There is no merit in the contention of the Noticee and the same is liable to be rejected.

6. DECISION OF THE COMMITTEE ON FIRST VIOLATION AS ALLEGED IN THE SCN AND SUBSUMED IN THE SSCN

a) *In view of the above, the Committee notes that the violations alleged in the SSCN which subsumes the violation alleged in the SCN stand established and the Noticee has failed to present any acceptable defense to the same. It stands established that the Noticee incorrectly reported in MG12 the TMs proprietary collateral / margin collected and available with the Noticee in the said six instances for 3 trading members as set out in Annexure A of NCL's letter dated September 22, 2022.*

Therefore, the penalty for false reporting stipulated by SEBI vide its circular dated August 10, 2011 i.e. '6. If during inspection it is found that a member has reported falsely the margin collected from clients, the member shall be penalized 100% of the

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falsely reported amount along with suspension of trading for 1 day in that segment', will be applicable as under.

Date	***TM Name***	***Shortfall (Rs. In Crs.) as per Annexure A of SSCN***	***Penalties as per SEBI circular dated 10.8.2011 @ 100% (Rs. In Crs.)***
23-Jan-18	*V-RISE SECURITIES PVT LTD*	*1.02*	*1.02*
28-Aug-18	*RELITRADE STOCK BROKING*	*1.22*	*1.22*
19-Dec-18	*RELITRADE STOCK BROKING*	*0.71*	*0.71*
26-Mar-19	*GLOBALWORTH SECURITIES LIMITED*	*7.71*	*7.71*
23-Sep-19	*GLOBALWORTH SECURITIES LIMITED*	*10.77*	*10.77*
23-Oct-19	*GLOBALWORTH SECURITIES LIMITED*	*8.73*	*8.73*
	TOTAL	***30.16***	***30.16***

Rationalization of penalties proportionate to violation: -

SEBI's circular dated August 1, 2019, prescribed rationalization of imposition of fines for false reporting of margins by Clearing Member, the relevant extract is given below for ready reference. The provisions of the circular came into force from September 1, 2019.

'3. In order to rationalize and bring uniformity in the manner of imposition of fine for 'false/incorrect' reporting of margin vis-à-vis 'non-reporting' of margin, following guidelines are issued:

a. The Stock Exchanges and Clearing Corporations, in all segments, in consultation with one another, shall devise a standard framework for imposition of fine on the

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Trading Member/ Clearing Member for incorrect/false reporting and non-reporting of margin collected from the clients.

b. Considering the principle of 'proportionality', the fine shall be charged to the member based on the materiality of non-compliance done by the member which may include factors such as number of instances, repeated violations, etc. The amount of fine to be charged upon the member may extend to 100% of such false/incorrectly/non reported amount of margin and/or suspension of trading for appropriate number of days.'

In compliance with the above SEBI circular, NCL vide its circular dated December 19, 2019 prescribed a range of penalties based on proportion of the violation and how often it was repeated, and the penalty was also capped at Rs. 25 lakhs.

b) *Along with the monetary penalty, the said circular also prescribes that the member may be subjected to suspension for one day in the respective segment in case of "material" instances. The circular also provides that for all cases prior to and up to August 31, 2019, the penalty structure under the August 10, 2011 SEBI circular will apply – i.e., 100%.*

Therefore, as set out in the above table, the first 4 items being prior to August 31, 2019, 100% would be the applicable penalty and for the last 2 items, it would be capped at Rs. 25 Lakh, thus making a total of Rs. 10.91 crores (Rs. 10.66 crores +

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Rs. 0.25 crores). However, the Committee has decided to apply the principles of proportionality as per the Orders of the Hon'ble Securities Appellate Tribunal (Hon'ble SAT) referred to herein below.

c) *The Committee also notes the order of the Hon'ble SAT dated June 10, 2019 in the matter of M/s. GRD Securities Limited Vs. National Stock Exchange of India Limited, which related to the said SEBI circular dated 10.8.2011, and which, inter alia, held that :-*

> *"....*
> *11. However, we are not able to agree with the stand of SEBI and NSE that no discretion in imposition penalty can be exercised, once a violation is established.....*
> *Further, proportionality is a basic principle to be adhered to while interpreting any provisions relating to punishment where the consequences are serious.....*
> *Therefore, a violation which leads to a complete failure of the market or market integrity and a violation which has no impact on the market need to be distinguished in interpreting proportionality.*
>
> *...."*

d) *The Committee also noted the order of the Hon'ble SAT dated October 9, 2020 in the matter of M/s. Alice Blue Financial Services Pvt. Ltd Vs. National Stock Exchange of India Limited, which related to the said SEBI circular dated 10.8.2011 and the NCL circular dated 19.12.2019, and which inter alia held that: -*

> *"....Though we note that the NSE circular dated December 16, 2019 has categorically stated that its applicability is from September 1, 2019 only, proportionality as a principle and as held in our order in GRD Securities*

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(supra) has to be examined. Though in the case of grave violations the MCSGFC is empowered to reject the proportionality angle, it is imperative for the Committee to give justification for such rejection, and it cannot be done just mechanically or by stating that the violations are serious. This is the crux of the circular dated August 1, 2019 issued by SEBI in order to rationalize and to bring uniformity in the manner of imposition of fine / penalty for false /incorrect reporting of margin, non-reporting of margin etc. Since the impugned Order has been issued subsequent to the said SEBI Circular, on 20 June, 2020 (sic), the Committee was bound to abide by that Circular, in addition to our Orders in GRD Securities (supra).'

e) *In view of the SEBI circular dated August 10, 2011, August 1, 2019, NCL circular dated December 19, 2019 and Hon'ble SAT order in the matter of M/s. GRD Securities and M/s. Alice Blue, the Committee holds that it would be just and reasonable to apply the principles underlying the NCL circular dated December 19, 2019 even to the contraventions committed before that date and levy the penalty of Rs. 25 Lakh for all the 6 instances as set out in the above table. Thus, the total penalty is reduced from the applicable Rs. 10.91 Crores and rationalized to Rs.25 Lakhs.*

f) *The NCL circular dated December 19, 2019 also specifies that in addition to imposing penalty, the member may be suspended from trading for one day in case of material instances. The Committee notes that no case for suspension is made out and as such, does not suspend the Noticee.*

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III. DETAILS OF SECOND VIOLATION AS GIVEN IN THE SCN and SSCN

1. The second violation stated in the SCN was as below: -

Non-adherence to prudent risk management policies (Violation of Clause 1 and Clause 2 read with Clause 3(1)(b) and Clause 3(1)(c) of Chapter V of NCL Rules)

It is observed that in case of the trading member Anugrah, there were 17 instances where in spite of non-payment of MTM Loss and shortfall in collaterals and funds collected towards margins vis-a-vis the margin requirements on a regular basis and for a continuous period, the Noticee allowed Anugrah to keep the positions open and did not square off the positions. It merely kept Anugrah in Risk Reduction Mode and recovered the MTM Loss by liquidating the securities placed as collaterals for multiple number of days.

2. The Noticee's Initial Submissions and the findings of the Committee to the above violation are summarized herein below: -

2.1 All of the instances referred to in paragraph 4 (ii) once again pertain to Anugrah and are the subject matter of proceedings before the Hon'ble SAT. Since the matter relating to Anugrah is sub-judice and pending final determination by the

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competent authority, the same should be excluded from the purview of the present SCN.

With regard to the Noticee's submission above, the Committee notes that the submissions of the member with respect to Anugrah has been dealt with appropriately in the para 2.3 of II above. The Noticee is precluded from taking shelter under the pretext of the present legal proceedings pending with the Hon'ble SAT in a totally different context.

2.2 The allegation raised, on the face of it, does not indicate violation of any of the identified clauses of NCL's Rules. The allegation made does not amount to violation of any provision in the SCN as there is no legal requirement for a PCM to square off the positions instead of selling collateral considering that selling collateral is one of the ways available to a PCM to regularize the account of a TM to recover MTM losses. Additionally, the SCN itself admits that the Noticee duly recovered the shortfall by liquidating the collateral of the concerned TM, which is in fact one of the modes of recovering shortfall from a TM in case of MTM Losses. The SCN also admits that the concerned TM was kept in RRM during this period, i.e., no fresh positions were allowed to be taken by the TM. The very fact that such actions were taken clearly indicate that Noticee did in fact have in place a prudent risk management policy and the same was adhered to.

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The limits are set at a TM level on an aggregate basis based on the availability of collaterals from the TM. In the event a TM defaults in fulfilling its payment obligations towards margins or other dues, then the PCM is entitled to liquidate the collaterals placed by the TM with it. Whenever a TM fails to meet its pay-in obligation, the Noticee was entitled to adjust the pay-in obligations of such TM against the collateral available with it. This is made clear by a plain reading of Clauses 2(5), 2(8), 5(4) and 5(6) of the model CM-TM Agreement prescribed by NCL and NSE.

Rules, Regulations or Byelaws of NCL do not set out a step-by-step procedure in which the MTM losses of a TM are to be recovered.

A CM is entitled to recover the MTM losses either by liquidating collateral to meet the MTM losses or square off the open positions of the concerned TM. However, it is far more prudent, both from a regulatory and risk perspective, to first liquidate the collateral rather than close out positions for the following reasons: -

a) Squaring off loss making open positions, especially in a volatile market (as was the case in March- June 2020), would create an immediate pay-in obligation. Since the TM whose positions are squared off is already in default, it would mean that the CM is incurring a pay-in obligation on behalf of a TM even though the TM does not have sufficient margin.

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Moreover, squaring off open positions of a TM in such a situation creates a risk of a systemic default by a CM to NCL. Considering that liquidation of collateral is one of the appropriate mode available with the CM, in order to avoid the catastrophic effect squaring off of the open positions by a defaulting CM, Noticee was fully entitled to liquidate the collateral available with it to meet the MTM losses of a defaulting TM.

b) With particular reference to Anugrah, all positions taken by Anugrah were positions belonging to the end-clients of Anugrah. The CM collects margin from the TM on an aggregate basis. However, the open positions of a TM are ultimately open positions belonging to the end-clients of the TM. However, in case of a margin shortfall on account of MTM losses, it is impossible for a CM to ascertain on a real time basis whether a particular open position relates to an end-client who has suffered an MTM losses leading to margin shortfall. Thus, squaring off open positions on an immediate basis to recover margin shortfall would create a risk of squaring off positions of clients who have not actually suffered MTM losses. Such clients would not only lose their positions but will also suffer potential pay-in obligations on squaring off of their positions.

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c) Squaring off open positions would also require a CM to take a commercial call as to which particular open position should be squared off. This can lead to unnecessary disputes with the TM who is likely to raise an objection that the CM has squared off a potentially profitable open position.

The Noticee has quoted the decision of the Hon'ble SAT in the case of SMC Global Securities Ltd. versus Securities and Exchange Board of India to highlight the importance of margin requirements and liquidating collateral placed as margin has been recognized by the Hon'ble SAT.

With regard to the Noticee's submission above, the Committee noted that the Noticee has failed to address the charge levelled against the Noticee by demonstrating that well defined prudent risk management systems were in place at its end. Therefore, the Noticee cannot take a defence that NCL has not prescribed step by step procedure in which the MTM losses of a TM are to be recovered. That does not absolve the Noticee of its obligation to have a prudent well defined system of risk management to protect itself from client default. The risk management policy shall be well documented. However, the form and mode of collection are left to the discretion of the Noticee.

The Committee noted that NCL sought additional information from the Noticee vide its letter dated March 17, 2022 with regard to failure to follow prudent risk management

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policies. The Noticee refused to provide the information as requested and failed to cooperate with NCL which had given to the Noticee a further opportunity vide its letter dated September 22, 2022 to show that prudent risk management practices were followed uniformly across all trading members during the inspection period. However, for the sake of good order and to provide the Noticee a full-fledged opportunity to defend itself against the allegation of non-adherence to prudent risk management policies, it was decided that a SSCN be issued to the Noticee.

3 The NCL issued the SSCN into which it subsumed the violation alleged in this regard in the SCN and alleged, inter alia, as follows: -

Non-adherence to prudent risk management policies

Violation of Clause 1 and Clause 2 read with Clause 3 (1) (b) and Clause 3 (1) (c) of Chapter V of the NCL Rules

3.1 In order to review whether the Noticee has adhered to the prudent risk management practices, NCL vide its letters dated March 17, 2022 and September 22, 2022 sought additional clarification/information to ascertain systems and procedures put in place to ensure compliance with the following :-

a) Regulation 4.1 of the NCL Regulations (F&O) states that "every F&O Clearing Member has a continuing obligation to maintain margins at the

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level and for the period stipulated by the F&O Segment of the Clearing Corporation from time to time."

b) Clause 9.1 of NCL circular (download reference no. 34657) dated April 17, 2017, states that the "Initial margin shall be payable on all open positions of Clearing Members, up to client level, and shall be payable upfront by Clearing Members in accordance with the margin computation mechanism and/ or system as may be adopted by the Clearing Corporation from time to time.

Initial Margin shall include SPAN margins, premium margin, assignment margin and such other additional margins, that may be specified by the Clearing Corporation from time to time." (Emphasis Supplied)

c) Bye Law 1 of Chapter IX of the Bye Laws (F&O) of NCL states that "a clearing member shall demand from his constituent the margin he has to provide under the Rules, Bye Laws and Regulations in respect of the business done by him for such constituent."

d) In terms of clause 9.7 of the NCL circular (download reference no. 34657) dated April 17, 2017, "the initial and exposure margin shall be payable

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upfront by the clearing members. Members are required to collect initial margins from their client/constituents on an upfront basis.*"*

3.2 As noted above, the Noticee was under the obligation to ensure that margins are collected on an upfront basis from its trading members. The Noticee has submitted in its replies to NCL that it had regularized the shortfalls with a delay ranging from 1 day to 24 days.

3.3 The Noticee further submitted that "We would like to reiterate that inevitably there are certain instances when the MTM losses of a particular TM increase on account of market fluctuation. As a result, the upfront margin placed by the TM with the CM may not be sufficient to cover such MTM losses. Given the inherent volatility of the F&O segment, such losses are entirely outside the control of the CM.*"*

3.4 The Noticee is required to have adequate systems and procedures in place to ensure that it collects and maintains appropriate collaterals from its trading members at all points in time, till the positions remain outstanding. It would therefore appear that the Noticee failed to adhere to the prudent risk management policies.

4 The Noticee's Reply to the SSCN is summarized as follows**:** -

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4.1 No order was passed on the SCN. Since the SSCN was issued after considering the submissions previously made by Noticee in respect of and contained the final set of violations the Noticee was required to answer, the submissions made by Noticee at the hearing held on December 6, 2022 were restricted to the allegations in the SSCN since all other allegations raised in the previous communications/SCN stand satisfactorily explained. Should any order be passed on the SCN at this stage, the Noticee reserves its rights to object to the jurisdiction, authority and power to pass an order on the SCN.

With regard to the Noticee's submission above, the Committee noted that the violation alleged in the SCN have been duly subsumed into SSCN and appropriately dealt with in this order for clarity and to provide background for the issue of SSCN. The SSCN has been issued after considering all the written and oral submissions made by the Noticee.

4.2 Reliance placed on Regulation 4.1 of the NCL Regulations (F&O) and Clauses 9.1 and 9.7 of NCL circular (download reference no. 34657) dated April 17, 2017 is completely misplaced as the same are in respect of a CM's obligation to furnish and maintain margins with the Clearing Corporation. The SSCN does not contain any allegation that ECSL has failed to furnish or maintain margins with the NCL. ECSL's primary obligation is to place sufficient margin with the

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Clearing Corporation and ensure that it honours its settlement obligations. ECSL has ensured that it was always compliant with this obligation and has not fallen short of its margin obligations towards NCL during the relevant period.

With regard to the Noticee's submission above, the Committee noted that as per Bye Law 1 of Chapter IX of the Bye Laws (F&O) of NCL which states that a clearing member shall demand from his constituent the margin he has to provide under the Rules, Bye Laws and Regulations in respect of the business done by him for such constituent. Further, in terms of clause 9.7 of the NCL circular (download reference no. 34657) dated April 17, 2017, "the initial and exposure margin shall be payable upfront by the clearing members. Members are required to collect initial margins from their client/constituents on an upfront basis.". Hence, the Noticee was under the obligation to ensure that margins are collected on an upfront basis from its trading members.

4.3 It is reiterated that the 6 instances mentioned in the Supplementary SCN do not relate to failure of ECSL to collect upfront margin from the TM but relate to shortfall in margin that arose on account of MTM losses suffered by such TMs during trading or on account of fluctuation of securities valuation due to market volatility. ECSL has a prudent risk management policy in place to ensure that limits are provided to TMs with sufficient haircut on collaterals and adequate margin is collected from the TMs before execution of any trades. However, due

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to the volatility and fluctuation in the market, the MTM losses of a particular TM can rise, and the upfront margin placed by the TM with the CM may not be commensurate with the margin requirements. Such events are entirely beyond the control of a CM. The mere fact that a particular TM has suffered an MTM loss which results in erosion of margin can never amount to a violation of collection of upfront margins by a CM. In fact, the rules, regulations and byelaws of the Clearing Corporation give the Trading Member time till T+1 or T+2 depending on the segment to clear any margin shortfall/pay-in obligation.

The Committee observes that the Noticee has failed to acknowledge that the violation 2 of SSCN pertains to compliance with collection of upfront margin requirements upto the level of the client of the trading members. The same is also prescribed as per the format of the CM - TM Agreement, inter alia stipulates that: -

> "…..
> *3(1) The Clearing Member shall ensure that the Trading Member collects margins from it / his constituents on such basis as may be prescribed by the NSCCL from to time.*
> ……..

It is submitted that in the event the margin placed by a TM is eroded due to market volatility, ECSL takes necessary steps to curtail the impact as per the risk management policy and system which tracks all TM level risk. ECSL immediately calls upon the TM to make good its margin obligations and ECSL team reaches out to the concerned TM and informs the TM of the shortfall in its

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account. ECSL on ongoing basis engages with TMs and ensures that the required margins are collected from TMs. The TM is also asked to make good the shortfall and regularize its account. The TMs are further informed of the shortfall in their account in the form of a Daily Activity Statement that is sent to them by ECSL at the end of the trading day. The DAS specifically sets out the margin obligation that the TM is liable to make good. After being intimated of the margin shortfall, the account is regularized in one of the following ways: (i) TM brings in additional collateral; (ii) Value of the existing collateral rises in subsequent days; (iii) Positions are reduced by TM which leads to reduction in margin requirement. In the event the shortfall persists, and the TM does not regularize its account despite reminders, then ECSL takes appropriate steps in accordance with its risk policy which include placing the TM in Risk Reduction Mode, i.e., preventing the TM from taking any fresh positions, initiating liquidation of collateral, etc. In case the shortfall in the proprietary trading account of a TM persists, then ECSL immediately reports to NCL.

It is submitted that ECSL has taken all steps necessary to ensure that on all the 6 instances, the accounts were regularized by the TMs by meeting their margin requirements. The information on how the shortfall was regularized and the time period within which the same was regularized is available with NCL. As per its policy, in each of the instances where the TM suffered a margin shortfall, ECSL sent an email to the concerned TM with the Daily Activity Statement,

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Daily Margin and Limit Summary and Consolidated Report across segments. The documents set out the margin obligation shortfall of such TMs and require the TM to make good the margin obligation. There is nothing in the SSCN which suggests that ECSL has ignored/failed to take necessary steps to recover margin shortfalls from the concerned Trading Members in violation of the extant rules, regulations or byelaws.

It is submitted that Supplementary SCN erroneously relies on irrelevant provisions to allege that ECSL failed to adhere to the prudent risk management policies as it failed to collect upfront margins from its TMs and thus, has violated Clause 1 and Clause 2 read with Clause 3(1)(b) and Clause 3(1)(c) of Chapter V of NCL Rules. As enumerated hereunder, since the instances referred to in the Supplementary SCN relate to margin shortfall on account of MTM, the provisions relied upon in the Supplementary SCN do not apply to the present case as the same either relate to deposit of margin by a CM with the Clearing Corporation or collection of initial margins by the CM from its clients/constituents.

With regard to the Noticee's submission above, the Committee notes that the SSCN pertains to non-collection of upfront initial margins and its failure to put in place a well-defined prudent risk management policy, hence, the Noticee's submissions pertaining to MTM losses are not relevant to the said violations.

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4.4 The SSCN deals with Regulation 4.1 of NCL Regulations (F&O) Regulations and Clause 9.1 of the NCL 2017 Circular. The above provisions are in respect of the obligation of a CM to furnish margin to the Clearing Corporation. However, the Supplementary SCN does not contain any allegation that ECSL has failed to furnish or maintain margins with the NCL. ECSL's has ensured that sufficient margin was placed by it with the Clearing Corporation i.e., NCL and has always honored/complied with its settlement obligations.

The reliance placed on Bye Law 1 of Chapter IX of the Bye Laws (F&O) of NCL and Clause 9.7 of the NCL 2017 Circular is completely misplaced since they relate to the CM's obligation to collect initial margin from its constituents. It is submitted that for all the 6 instances mentioned in the Supplementary SCN, the margin shortfall was not on account of ECSL's failure to collect initial margins from the TMs but was in respect of the MTM loss suffered by the TM due to market fluctuations.

Since the aforesaid provisions are not in respect of collection of margin shortfall in respect of the MTM loss suffered by the TM, the allegation in the Supplementary SCN that Noticee failed to adhere to the prudent risk management policies is without any basis whatsoever.

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With regard to the Noticee's submission above, the Committee observed that the SSCN issued by NCL clearly spells out the responsibility of the Noticee with respect to the Clearing Corporation as well as with respect to its TM's. The Noticee was duty bound to collect the margin from its TM's, in terms of Bye law 1 of chapter IX, which the Noticee was required to provide to NCL in terms of Regulation 4.1. The Committee notes that since all the instances of shortfall as referred to in the SSCN relate to shortfall in collection of the margins which were required to be collected on an upfront basis and do not pertain to MTM losses, the Noticee failed to adhere to prudent risk management practices. The Noticee should have adequate systems and procedures in place to ensure timely collection of upfront initial margin from its TM's to protect itself against default by the TM's.

5 DECISION OF THE COMMITTEE ON SECOND VIOLATION AS ALLEGED IN THE SCN AND SUBSUMED IN THE SSCN

In the facts of the present case, the Committee observes that the Noticee has failed to demonstrate that well defined prudent risk management systems and procedures are in place. The Committee therefore concludes that it would be appropriate to issue a reprimand to the Noticee with a direction to put in place well defined prudent risk management systems and procedures to ensure that its Trading Member collects margins from its clients as may be prescribed by the NCL from time to time.

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IV. DETAILS OF THIRD VIOLATION AS ALLEGED IN THE SCN

1. The third violation alleged in the SCN is as follows: -

Non-adherence to Exchange's circular NSE/INSP/41359 dated June 20, 2019, Exchange's circular NSE/INSP/42000 dated August 29, 2019, Exchange's circular NSE/INSP/42052 dated September 4, 2019, and NCL circulars NCL/CMPL/41442 dated June 28, 2019 and NCL/CMPL/42015 dated August 30, 2019)

It was observed that the Noticee had not closed one of its beneficiary accounts (IN303719-11047823) within the given time frame as required by the aforesaid NSE and NCL circulars.

2. The Notice's Reply in its Initial submissions is summarized herein below: -

2.1 As per clause 5 of the SEBI Circular No. CIR/HO/MIRSD/DOP/CIR/P/2019/75 dated June 20, 2019 ("SEBI June 2019 Circular"), all existing client securities accounts opened by a TM/CM were required to be wound up on or before August 31, 2019. The implementation of clause 5 of SEBI June 2019 Circular was further extended to September 30, 2019 vide SEBI circular No. SEBI/HO/MIRSD/DOP/CIR/P/2019/95 dated August 29, 2019. NSE vide its Circular No.27/2019 further issued a clarification that all securities lying in the existing Stockbroker-Client Accounts shall be either returned to the clients upon

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fulfilment of pay-in obligation or disposed-off after giving notice of 5 days to the client, on or before September 30, 2019

2.2 ECSL in compliance with the SEBI, NSE and NCL Circulars, opened the requisite beneficiary accounts in September 2019 which were required to be maintained post October 1, 2019. The securities lying in the Account, which was a "Stockbroker-Client Account", were dealt with in accordance with the aforesaid circulars by September 30, 2019 and account had NIL securities on such date. The process for closing the Account was initiated and the Account was thereafter closed by ECSL on October 11, 2019. Despite delay of 8 working days in closing the Account, the Account was not used after October 1, 2019.

2.3 A copy of the statement of account evidencing that no securities are lying in the said account as on September 30, 2019 has been provided by the Noticee.

2.4 Thus, even if it is assumed that the delay in closure even of an account not having any securities or trades was a breach, it was at best merely a technical or venial breach. In this regard it is pertinent to note the view taken by the Hon'ble Supreme Court in Hindustan Steel Ltd. versus State of Orissa[5]

"8. ...Penalty will also not be imposed merely because its lawful to do so. Whether penalty should be imposed for failure to perform a statutory obligation is a matter of discretion of the authority to be exercised judicially an on a consideration of all the relevant circumstances. Even if

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a minimum penalty is prescribed, the authority competent to impose the penalty will be justified in refusing to impose penalty, when there is a technical or venial breach of the provisions of the Act…"

3. **FINDINGS OF THE COMMITTEE IN RESPECT OF THE THIRD VIOLATION AS ALLEGED IN SCN: -**

3.1 The Committee noted that the due date for closure of the demat account as per SEBI defined timelines was September 30, 2019.

3.2 The Committee further noted that the demat account No. IN303719-11047823 had NIL balance as on September 30, 2019. The Noticee initiated the process for closing the account and the account was thereafter closed on October 11, 2019. The Noticee has submitted that the account was not used after October 1, 2019.

3.3 *The Committee noted that although there were no securities in the account as on September 30, 2019 and no securities were credited thereafter, the same is not a justification for not closing the account within the stipulated time - i.e. by September 30, 2019. The Committee also noted that in its order dated September 29, 2022, this Committee has approved the levy of a penalty of Rs.50,000/- in respect of the same demat account, for non-compliance observed during a joint inspection of the Noticee conducted by SEBI, for which enforcement was delegated to NCL. The said penalty has been collected from the Noticee.*

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Therefore, the Committee noted that the Noticee cannot be penalized twice for the same non-compliance and hence the Committee has decided not to impose any further penalty.

V. FINDINGS OF THE COMMITTEE ON THE OTHER SUBMISSIONS OF THE NOTICEE

The Committee has ensured that in the present proceedings all requisite principles of natural justice are fully complied with. The Committee has granted extensions of time, postponement of personal hearings etc., as requested by the Noticee on all occasions. Full and unrestricted opportunities were given to the Noticee to make its written and oral submissions as requested by the Noticee. The Committee is of the view that the Noticee's allegation of violation of basic rules of nature justice is totally bald, baseless, false and belied by the record. The Committee also noted that the Noticee was not cooperative in submitting the information called for by NCL. Perhaps the whole exercise could have been avoided if the Noticee had submitted the available information and explained what corrective steps it proposes to take. The Committee noted that the Noticee is subject to the regulatory jurisdiction of the NCL. Noticee cannot evade disclosure of information and documents on such grounds as 'fishing inquiry' etc. The Committee expects the Noticee to be co-operative and transparently furnish the information and documents that may be called for by the NCL in future.

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DECISION

1) For violation 1 as per SSCN relating to incorrect reporting under MG 12 for Trading Member's proprietary margins obligations, the total penalty is reduced from the applicable Rs. 10.91 Crores and rationalized to Rs. 25 Lakh, is levied in terms of SEBI circular no. CIR/DNPD/7/2011 dated August 10, 2011 and SEBI circular no. CIR/HO/MIRSD/ DOP/CIR/P/2019/88 dated August 1, 2019 read with NCL circular no. 42946 dated December 19, 2019, considering the principle of proportionality as set out in the Hon'ble SAT's judgment dated June 10, 2019 in the matter of *M/s.* GRD Securities Limited and its judgment dated October 9, 2020 in the matter of *M/s.* Alice Blue Financial Services Pvt. Ltd.

2) For violation 2 as per SSCN relating to non-adherence to prudent risk management policies, the Noticee is reprimanded with a direction to put in place well-defined prudent risk management systems and procedures to ensure that its Trading Member collects margins from its clients as may be prescribed by the NCL.

3) For violation 3 as per SCN relating to non-closure of one beneficiary demat account, the Committee decided not to levy any further penalty for the reasons as mentioned above.

4) The aforesaid penalty of Rs. 25 lakhs for the first violation shall be payable by the Noticee within a period of 15 days from the date of this order. In case the Noticee fails to pay the aforesaid penalty, the said amount shall be recovered from the

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proprietary collateral of the Noticee available with NCL on the next working day immediately following the date of expiry of the aforesaid period of 15 days or soon thereafter.

Sd/-	Sd/-	Sd/-	Sd/-	Sd/-
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G S Hegde	**Bhagyam Ramani**	**Jayant Haritsa**	**Vikram Kothari**	**Golaka C Nath**
(Chairperson)	**(Committee Member)**	**(Committee Member)**	**(Committee Member)**	**(Committee Member)**

The Committee has given confirmation on email instead of physical signatures

Date: March 31, 2023

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