CGM/AA/QJC-1/IMD/IMD-II_DOF7/21673/2022-23

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

UNDER SECTION 12 (3) OF THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 READ WITH REGULATION 27 OF THE SECURITIES AND EXCHANGE BOARD OF INDIA (INTERMEDIARIES) REGULATIONS, 2008 IN RESPECT OF KARVY STOCK BROKING LIMITED, [PAN No.: AABCK5190K] [SEBI REGISTRATION NO.: INP000001512].

FACTS OF THE CASE

1. Securities and Exchange Board of India (hereinafter referred to as "**SEBI**") conducted inspection of M/s Karvy Stock Broking Limited (hereinafter referred to as "**the Noticee/ PMS-Karvy/ the Company**"), a registered Portfolio Manager (SEBI with Registration No. INP000001512) with respect to its portfolio management activities from December 05, 2019 to December 13, 2019. The period covered in inspection was from April 01, 2018 to March 31, 2019 (hereinafter referred to as "**inspection period**").

2. The findings/ observations made during the course of inspection were communicated to the Noticee by SEBI vide letter dated June 22, 2020. The Noticee filed its reply vide letter dated August 09, 2020. Thereafter, SEBI initiated enquiry proceedings against the Noticee under Chapter V of SEBI (Intermediaries) Regulations, 2008 (hereinafter referred to as "**Intermediaries Regulations**") for the alleged violations of various provisions of SEBI (Portfolio Managers) Regulations, 1993 (hereinafter referred to as "**Portfolio Managers Regulations, 1993**") and applicable SEBI Circulars as stated below:

Sr. No.	Alleged Violations	Regulatory Provisions
1	Failure to appoint appropriately qualified or experienced Principal Officer	Regulation 6(2)(c) of Portfolio Managers Regulations, 1993
2	Contrary provisions in regard to placement fee in the Disclosure Document	Regulation 13 of Portfolio Managers Regulations, 1993 read with clauses 1 and 9 of Schedule III of Portfolio Managers Regulations, 1993
3	Provisions in the Portfolio Management Agreement with regard to outsourcing of core activities	Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 of Schedule III (Code of Conduct) of Portfolio Managers Regulations, 1993 and Clause 5 of SEBI Circular CIR/MIRSD/24/2011 dated December 15, 2011
4	No uniformity in provisions of termination of agreements with clients	Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 and 3 of Schedule III of Portfolio Managers Regulations, 1993
5	Non provision of details of penalties, pending litigation or proceedings, findings of inspection or investigations for which action may have been taken or initiated by any regulatory authority against	Regulation 14(2)(a) of Portfolio Managers Regulations, 1993 read with sub-clause 4, Clause III of the Model Disclosure Document for Portfolio Management in Schedule V of Portfolio Managers Regulations, 1993 and Clause 3(b) of SEBI

	PMS-Karvy, in the Disclosure Document.	CIRCULAR Cir. /IMD/DF/16/2010 dated November 02, 2010
6	Open positions in respect of allocation of purchases of securities effected in a day	Regulation 16(5) of Portfolio Managers Regulations, 1993
7	Non- rectification of deficiencies made in internal auditor's report within two months of receipt of audit report half year ended September 30, 2018 and March 31, 2019	Regulation 15 (2) of Portfolio Managers Regulations, 1993 read with Clause 8 of Schedule IV of Portfolio Managers Regulations, 1993 and Regulation 22 of Portfolio Managers Regulations, 1993
8	Failure to appoint qualified or experienced Compliance Officer and failure to report non-compliance in regard to appointment of Principal Officer by the Compliance Officer	Regulations 23A(1) and 23A(2) of Portfolio Managers Regulations, 1993
9	Failure to provide correct information to SEBI in regard to disposal dates of complaints filed by its clients with PMS-Karvy and non-maintenance of proper records pertaining to redressal of complaints	Regulation 9A(1)(c) read with regulation 15(6) of Portfolio Managers Regulations, 1993

APPOINTMENT OF DESIGNATED AUTHORITY

3. A Designated Authority (hereinafter referred to as the **'DA')** was appointed by SEBI vide communique dated October 21, 2021 under Section 19 of the SEBI Act, 1992 read with Regulation 24 of the Intermediaries Regulations, to enquire

into the violations of aforesaid provisions alleged to have been committed by the Noticee and submit the Report in terms of Section 12 (3) of the SEBI Act, 1992 read with Regulation 23 and 26 of Intermediaries Regulations, 2008.

4. Pursuant to an enquiry, the DA vide an Enquiry Report dated May 26, 2022, in terms of Regulation 26(1)(iii) of the Intermediaries Regulations, recommended that the certificate of Registration granted to Karvy Stock Broking Limited as portfolio manager having SEBI Registration No. INP000001512 may be suspended for a period of three months.

SHOW CAUSE NOTICE, REPLY OF THE NOTICEE AND HEARING

5. Thereafter a Post Enquiry Show Cause Notice No. EFD/DRA4/AA/AP/OW/26823/1/2022 dated June 30, 2022 (hereinafter referred to as **"SCN"**) enclosing therewith the Enquiry Report, was issued to the Noticee advising it to show cause as to why the action as recommended by the DA or any other action including passing appropriate directions as deemed fit by the Designated member, should not be imposed on it.

6. The SCN was duly served on the Noticee. No reply was received from the Noticee. Reminders for filing replies were sent to the Noticee. In the interest of natural justice, the Noticee was granted opportunities of hearing vide notices dated September 08, 2022, October 04, 2022, November 02, 2022 and November 15, 2022 respectively. The Noticee is also granted opportunities for filing detailed reply/additional written submissions 3 days before the scheduled date(s) of hearing. However, the Noticee did not appear on the scheduled dates for hearing. The Noticee was seeking adjournments on all occasions, either on the day scheduled for hearing or just a day before the scheduled date of hearing citing different reasons as mentioned below:

Sr. No.	Date/Hearing Date	Description	Response from the Noticee
1.	June 30, 2022	Post Enquiry Show Cause Notice was issued to PMS-Karvy on June 30, 2022.	PMS-Karvy has not replied to the SCN till November 21, 2022.
2.	September 23, 2022 at 03:00 PM	**1st Hearing Notice** was issued to PMS-Karvy **on September 08, 2022.**	Shri V Mahesh, MD of Karvy Data Management Services Ltd. vide email dated **September 23, 2022 (on the date of hearing**) has requested 4 weeks' time to gather the data so as to enable the legal counsel to respond to SEBI.
3.	November 02, 2022 at 03:00 PM	**2nd Hearing Notice** was issued to PMS-Karvy **on October 04, 2022.**	The legal counsel vide email dated **November 01, 2022** (**one day before hearing date**) requested for further adjournment for another 1 month on the grounds of health issue of one of the Director of PMS-Karvy, Mr. C. Parthasarthy, that too one day prior to the hearing.
4.	November 14, 2022 at 3:00 PM	**3rd Hearing Notice** was issued to PMS-Karvy **on November 02, 2022.**	The legal counsel vide email dated **November 14, 2022 (on the date of hearing date)** informed that the Senior Counsel would not be able to appear before the Quasi-Judicial Authority today "*due to an urgent hearing matter before the Hon'ble High Court at Hyderabad*". On the aforesaid ground, the entity has

			sought adjournment of the hearing in the matter, and, has **undertaken and confirmed that no further extension of time shall be sought** in this regard.
5.	a) For November 15, 2022: Any time between 11:00 am to 1:00 pm b) For November 16, 2022: Any time between 11:00 am to 5:00 pm c) For November 17, 2022: Any time between 11:00 am to 5:00 pm	**4th Hearing Notice** was issued to PMS-Karvy on **November 15, 2022**. PMS-Karvy has been granted the liberty to decide the exact date and time of appearance from among date mentioned.	Shri V Mahesh has informed on November 16, 2022 (**on the date of hearing date**) that the advocate is going to withdraw the brief of the case to represent PMS-Karvy. On account of this precarious position, he requested that KSBL be provided at least 7 - 10 days so that an advocate can be identified for representing them.

In the interest of principles of natural justice, the Noticee was granted last and final opportunity of hearing vide notice dated November 21, 2022. It was advised to appear before the undersigned on November 25, 2022. M/s Vis Legis Law Practice, the Authorized Representative (hereinafter referred to as '***AR***') of the Noticee submitted a detailed reply dated November 23, 2022 to the SCN received on November 24, 2022. On November 25, 2022, the AR requested for online hearing. The same has been acceded to. The hearing was conducted on November 25, 2022 at 3PM through Video Conference mode on Cisco Webex wherein the AR appeared for the Noticee and made his submissions. The AR also requested time for filing additional written submission till November 28, 2022. The AR vide email dated November 27, 2022 filed a short written submission in addition to its earlier reply dated November 23, 2022.

7. The noticee vide its letter dated November 23, 2022 *interalia* submitted the following in its reply to the SCN:

"Appointment of Principal Officer

1. *With reference to **Paras 10 to 15** of the Enquiry Report following be noted:*

(a) *The DA has failed to appreciate the explanations given by our Client and also the circumstances under which Mr. Vikas Rajpal (-who is alleged to be not adequately qualified or experienced for being designated/appointed as Principal Officer),was appointed as Principal Officer of PMS-Karvy. At the relevant time, many of our employees had resigned from KSBL, including the then Principal Officer Mr. Rupin Shah -who had resigned from the Company with immediate effect. Post resignation of Mr. Rupin Shah, our Client was in the process of hiring an appropriately qualified / experienced person and the same took some time. Due to absence/non availability of a qualified or experienced person, Mr. Vikas Rajpal was given the position of Principal Officer in the interest of investors as a temporary arrangement. Subsequently, Mr. Sachin Mittal, who was admittedly duly qualified and experienced for the position, was appointed as Principal Officer in June, 2020. The said appointment took some time due to non-availability of right/suitable candidate with requisite qualifications/experience.*

(b) *Admittedly, there is no adverse finding by the DA, that as a consequence of aforesaid temporary arrangement, the needs or the interests or the rights of the investors or the interest of the securities markets, was compromised in any manner, or that the matters pertaining to the clients were not handled efficiently. Admittedly, there are no client complaints.*

(c) *Further, the DA has also failed to appreciate our submission viz. that the PMS Regulations 2020 have relaxed the requirement of experience for Principal officer in the securities market from 10 years to 5 years and Mr Vikas Rajpal*

had experience of around 7.5 years. In fact, the DA has also accepted that Mr. Vikas Rajpal was having experience of around 7.5 years as portfolio manager, investment advisor and fund manager and had certification from NISM Series XV Certified Research Analyst. But the DA has refused to grant benefit of amended provisions, by resorting to convenient hyper-technicalities viz. provision applicable at the relevant time will only be applicable, completely ignoring that the subsequent amended provisions had mollified the rigour of earlier law by relaxing the qualification requirements in terms of duration of experience.

(d) *We therefore deny that our Client has violated provisions of regulation 6(2)(c) of PMS Regulations, as alleged. In any event, the alleged violation, in the facts and circumstances of the case is, at the highest a technical, procedural and venial violation, with no consequential impact on clients or the securities market in any manner.*

Contrary provisions in disclosure documents

2. *With reference to **Paras 16 to 23** of the Enquiry Report following be noted:*

(a) *The DA has failed to appreciate the explanations given by us with regard to alleged contrary provisions in the Disclosure Document, specifically that it was purely an error of inadvertence.*

(b) *We submit that earlier, our Client was charging the placement fee from its clients upfront. Subsequently, during 2016-17considering various representations from clients to deduct charges on a quarterly basis, in the interest of the clients, our Client had changed the time period of charging placement fee in Annexure A- Section II of the disclosure documents. Since FY 2016-17 placement fees was being charged on a quarterly basis spread over one year uniformly to all clients (which was more advantageous and convenient to the clients), instead of upfront fees. Inadvertently, while acceding to the*

representations of the clients, the concomitant change was not carried out, at the relevant time, in Section 10 of the disclosure documents. Same was nothing but an error of inadvertence. Here it may be appreciated that, it is nobody's case that no placement fees is to be paid by the clients. Only issue, arising from the alleged disclosures, is when i.e. whether upfront or over a period of time over 1 year.

(c) *The said inadvertent error cannot be elevated to the status of "negligence" as sought to be done by the DA, especially since the same was innocuous lapse with no adverse consequence on the clients' interests*

(d) *Admittedly, there is no adverse finding by the DA, that as a consequence of alleged contrary provisions in Disclosure Document, our Client has compromised the interests or the rights of the investors or the interest of the securities markets in any manner. Merely because there was inadvertent error, which had no consequential impact, it cannot be alleged that: (a) our Client has failed to observe high standards of integrity and fairness in our dealings or; (b) that our Client has not given true and adequate information to investors and clients or; (c) that our Client has made any misguided claims or; (d) that our Client has not dealt in a prompt, efficient and cost effective manner. Admittedly, there are no client complaints.*

(e) *We therefore deny that our Client has violated provisions of regulation 13 of PMS Regulations read with clauses 1 and 9 of Schedule III, as alleged. In any event, the alleged violation, in the facts and circumstances of the case is, at the highest a technical, procedural and venial violation, with no consequential impact on clients or the securities market in any manner.*

Provisions of outsourcing of core activities in Model Portfolio Management Agreement

3. *With reference to **Paras 24 to 30** of the Enquiry Report following be noted:*

(a) *The DA has failed to appreciate the explanations given by our Client with regards to alleged outsourcing of core activities. Clearly, there is no provision in the Portfolio Management Agreement with regard to outsourcing of core activities. We specifically and categorically state that our Client has not outsourced the core activities to anyone. The allegation is premised on out-of-context reading of Clause 2.18 of the Agreement, which has been given an expansive and distorted meaning, which was never contemplated or intended by our Client.*

(b) *At all points of time, actual core activities, including, picking the stocks for investment, timing of the investment, price at which investments are to be made, quantum of investments to be made etc was exclusively decided by the Portfolio Manager. Intent behind the alleged Clause No 2.18 in the Agreement was to delegate only the routine and incidental operational activities pertaining to investment decisions (viz. interacting with other intermediaries such as Brokers, AMC's etc on Client's behalf to facilitate the transactions in the portfolio, to provide for appointment of custodian, to seek best fund accounting services etc as and when required) so as to maintain speed and efficiency in operations.*

(c) *Till date our Client has not received any complaint from any of our client stating that our core activities as a portfolio manager was outsourced to other agencies. Even the inspecting officials in their Report have inter alia recorded that " It is, however, observed that the core activities have not been outsourced as on date of inspection" (Refer Pg 16 of Report on Inspection). Said observations also reinforce our contention that Clause No 2.18 in the Agreement has been read out of the context and that our Client has never outsourced our core activities. Additionally, DA has failed to appreciate that the embargo is only on outsourcing of "core activities" and not on other activities.*

(d) *In the Enquiry Report, though the DA has itself recorded that "Though the Noticee did not outsource its core activities" but has erred in observing that "keeping such provision in the agreement allows the Noticee to do so which is against the integrity and fairness on part of the Noticee". The DA has resorted to hypothetical possibilities, while interpreting the clauses with a jaundiced eye .The DA has failed to appreciate the underlying spirit behind the clause, and based on hair-splitting arguments returned adverse findings against our Client, which is legally untenable and unsustainable.*

(e) *We therefore deny that our Client has violated provisions of Regulation 13 read with Clause I of Schedule III (Code of Conduct), Clause 5 of SEBI Circular CIR/MIRSD/24/2011dated December 05, 2011, as alleged. We further deny that our Client has not observed high standards of integrity and fairness in all our dealings with our clients as alleged.*

Failure to maintain uniformity in provisions for termination of agreement with clients

4. *With reference to **Paras 31 to 37** of the Enquiry Report following be noted:*

(a) *The DA has failed to appreciate the explanations given by our Client with regard to the allegation pertaining to failure to maintain uniformity in provisions of termination of agreements with Clients, wherein our Client had fairly accepted that there is lack of uniformity in Clauses 12.4 & 12.5 of the Agreement and that same was an inadvertent error.*

(b) *The DA has failed to appreciate that our Client had never terminated/suspended any client's account immediately/without prior notice except in circumstances such as death of the client or the client being banned by SEBI etc. Further, even there is no finding that our Client had terminated/suspended any client's account immediately/without prior notice. It is quite pertinent to note that our*

Client had not received any complaint from any of our client stating that our Client had terminated/suspended their accounts unilaterally by issuing a written notice of termination.

(c) *Admittedly, even there is no finding in the Enquiry Report that our Client has terminated the Agreement unilaterally with the client without any notice, to his disadvantage taking recourse to Clause 12.4 of the Agreement. Merely because there was inadvertent error, which had no consequential impact, it cannot be alleged that: (a) our Client has not rendered high standards of service or; (b) that our Client has not exercised due diligence and independent professional judgement or; (c) that our Client has not ensured fair treatment to clients or; (d) that our Client has placed our interest above those of the clients, as alleged.*

(d) *We therefore deny that our Client has violated provisions of Regulation 13 of PMS Regulations, 1993 read with Clauses 1 and 3 of Schedule III , as alleged. In any event, the alleged violation, in the facts and circumstances of the case is, at the highest a technical, procedural and venial violation, with no consequential impact on clients or the securities market in any manner.*

Failure to provide certain details in Disclosure Document

5. *With reference to* ***Paras 38 to 44*** *of the Enquiry Report following be noted:*

(a) *The DA has failed to appreciate the explanations given by our Client with regards to the allegation pertaining to failure to provide certain details in the disclosure documents. Our Disclosure Document, as uploaded on the website at the relevant time had contained the details of penalties, pending litigation or proceeding, findings of inspection or investigations of which action may have been taken or initiated by any regulatory authority. In the said Disclosure Document, at Annexure B/Pg 54, all the relevant particulars pertaining to the*

details of penalties, pending litigation or proceeding, findings of inspection or investigations of which action may have been taken or initiated by any regulatory authority, had been set out. Same was also pointed out during the inspection to the SEBI Officer's.

(b) *The DA has failed to appreciate that even the SEBI Inspection Report rightly observes that our Client has been communicating the disclosure requirement to the clients before entering into the agreement. We reiterate that all points of time our Client has transparently disclosed everything, to the clients as mandated by SEBI and not hidden or suppressed anything from them.*

(c) *Admittedly, it is not DA's case that details of penalties, pending litigation or proceeding, findings of inspection or investigations of which action may have been taken or initiated by any regulatory authority, was not made known to the investors/clients. Hard copies of the disclosures were made available to the investors/clients at the time of execution of Agreement. Limited allegation is that the details were not placed on the our Client's website. Same was an inadvertent error, with no consequential impact.*

(d) *We therefore deny that our Client has violated provisions of Regulation 14(s2)(a) read with Clause IV of Schedule V of SEBI (PMS) Regulations, 1993 and Clause 3(b) of SEBI Circular No. Cir/IMD/16/2020 dated November 02, 2010, as alleged. In any event, the alleged violation, in the facts and circumstances of the case is, at the highest a technical, procedural and venial violation, with no consequential impact on clients or the securities market in any manner.*

Open positions in respect of allocation of purchase of securities effected in a day

6. *With reference to **Paras 45 to 49** of the Enquiry Report following be noted:*

(a) *The DA has failed to appreciate the explanations given by our client with regard to the allegation pertaining to open positions, wherein our Client had inter alia submitted that, the open positions was kept in respect of allocation of securities on 23-07-18 and 24-07-18. The same occurred due to the operational lapse, from our side. Said lapse was purely unintentional and an error of inadvertence.*

(b) *The DA has failed to appreciate that during the entire Inspection Period spanning over 1 year (i.e. from April 01, 2018 to March 31, 2019) only on few stray days there was open position in respect of allocation of securities. On the remaining days there is no open position in respect of allocation of securities. It may be noted that the quantum of pen positions is exceedingly insignificant.*

(c) *It may be noted that the alleged positions remained open (during a limited period) inter alia due to attrition during the relevant time, wherein employees had left, which was sorted out by hiring fresh employees in July 2018, and whereafter there was no such issue. It is pertinent to note that no complaints have been received by our Client from our clients in this regard. Said lapse was purely unintentional and an error of inadvertence.*

(d) *We therefore deny that our Client has violated provisions of Regulation 16(5) as alleged. In any event, the alleged violation, in the facts and circumstances of the case is, at the highest a technical, procedural and venial violation, with no consequential impact on clients or the securities market in any manner.*

Non rectification of deficiencies mentioned in Auditors Report

7. *With reference to* ***Paras 50 to 55*** *of the Enquiry Report following be noted:*

(a) *The DA has failed to appreciate the explanations given by our Client with regard to the allegation pertaining to non-rectification of deficiencies mentioned in the Auditors Report. The alleged differences-which are minimal and involve insignificant amount vis-à-vis the total amounts handled by PMS-Karvy, have*

arisen, due to operational reasons viz non identification of the individual clients to whom such balances pertained. Therefore, our Client our was not in a position to rectify the audit observation.

(b) *We may also point out that, after efforts to reconcile the balances did not materialise, there was lack of clarity as to how to treat this amount. Finally, it was decided that the amounts should be transferred pro rata to the accounts of all investors belonging to the particular schemes. However, before our Client could implement our decision our bank account was frozen. It may be noted that during April 2021, our Client's bank accounts were frozen pursuant to directions issued by The National Stock Exchange.*

Failure to appoint appropriate Compliance Officer

8. *With reference to* ***Paras 56 to 62*** *of the Enquiry Report following be noted:*

(a) *The DA has failed to appreciate the explanations given by our Client with regard to the allegation pertaining to appointment of appropriate Compliance Officer.*

(b) *As stated hereinbefore, the appointment of the Principal officer/Compliance officer was made under peculiar circumstances, wherein during the year 2018 - 19 many of our employees had resigned from KSBL, including the then Principal Officer Mr. Rupin Shah -who had resigned from the Company with immediate effect. Post resignation of Mr. Rupin Shah, our Client was in the process of hiring an appropriately qualified /experienced person and the same took some time and under the aforesaid circumstances, our Client had, keeping the interest of investors in mind, identified and appointed an existing staff member Mr Vikas Rajpal as Principal Officer/Compliance Officer. It is submitted that during that time he was the only officer whose qualification and experience was close to the requirements of a Principal Officer/Compliance officer, as prescribed by SEBI. Subsequently, in July 2020 our Client had appointed Mr Shankhadeep Nath as the Compliance Officer.*

(c) *Admittedly, there is no adverse finding by the DA, that as a consequence of appointment Mr Vikas Rajpal as Principal Officer/Compliance Officer, the needs or the interests or the rights of the investors or the interest of the securities markets, were compromised in any manner.*

(d) *We therefore deny that our Client have violated provisions of regulation 23A(1) of PMS Regulations, as alleged. In any event, the alleged violation, in the facts and circumstances of the case is, at the highest a technical, procedural and venial violation, with no consequential impact on clients or the securities market in any manner.*

Failure to maintain and provide proper information of redressal of complaints

9. *With reference to **Paras 63 to 67** of the Enquiry Report pertaining to information of redressal of investor complaints, the DA has accepted that the allegation is untenable. In the Enquiry Report, DA has specifically observed that "I find that the violation of provisions of regulation 9A(1)(c) read with Regulation15(6) of Portfolio Managers Regulations, 1993, does not stand established".*

10. *With reference to **Paras 68** of the Enquiry Report, our Client reiterates the submissions made in the earlier paras, since the same is repetition and summarisation of the allegations made in the Enquiry Report.*

11. *With reference to **Paras 69** of the Enquiry Report, our Client reiterates that the DA has failed to appreciate our submissions in proper perspective and to consider the matter holistically keeping the interest of investors/clients in the forefront, and also the vital fact as to, whether in effect any damage has actually been caused to the interest of investors/clients or is it a mere paper violation. The adverse recommendation made by the DA is, oppressive, harsh and excessive, apart from being exceedingly disproportionate. It is true that purpose of "the said*

provisions is to deter the wrong doing and promote ethical conduct in the securities market", but the provisions have to be invoked responsibly and in a fair and reasonable manner."

8. The noticee vide its email dated November 27, 2022 *interalia* submitted its reply to the SCN that the alleged lapses pointed out in the Enquiry Report are merely technical, procedural, and venial in nature, and that they had no impact whatsoever on their Clients' interests in any manner. There are, admittedly, no investor complaints arising from the alleged technical breaches as stated in the Notice. The Noticee submitted that at all points in time they had acted bonafide, rendered best possible services to their clients and taken care of their clients interest, which would also be fortified and reinforced by the following observations in the Inspection Report. They also cited certain findings from the Inspection Report that:

8.1. *Para ix /Pg 18 of Inspection Report*

8.1.1. PMS-Karvy has kept funds of all clients in a separate account maintained with Scheduled Commercial Bank i.e. Kotak Mahindra Bank Ltd.

8.1.2. PMS-Karvy has not derived any direct and indirect benefit out of the clients' funds and securities. Further, it has not borrowed funds and securities on behalf of the client. PMS-Karvy has not lent securities on behalf of the clients to any third person".

8.2. *Para xii /Pg-20 of Inspection Report*

8.2.1. the records have been maintained in compliance with the regulation like Balance sheet, Profit and loss account, Auditor's report, Statement of financial position and Investment rationale for the trades etc

8.3. *Para xiv /Pg-20 of Inspection Report*

8.3.1. PMS-Karvy has maintained separate client-wise accounts.

A certificate for compliance with Regulation 20(2) has been furnished with the half yearly report for the period ended on 31st March, 2019.

The same has been communicated to clients to their respective emails. No client has appointed a Chartered Accountant during the inspection period to audit the books and accounts of the portfolio manager relating to his/her respective transactions"

8.4. *Para xv /Pg-20 of Inspection Report*

8.4.1. PMS-Karvy provides monthly reports and half yearly reports to the clients which includes portfolio snapshot statement, portfolio holdings, realized gain/loss statement, transaction listing report, expense report and details of beneficial interest received.

9. The Noticee stated that there is no finding against it that while making investment decisions on behalf of their clients, they have not acted professionally or; acted in a fraudulent and unfair manner; or has enriched themselves at the expense of their clients or; has leveraged on the basis of their clients funds or securities.

10. The Noticee also submitted that the recommendation of suspension is egregious and drastic. Given the facts of the case and the nature of the alleged violations, with absolutely no impact on the clients' interests, no client complaints, and express observation of the Inspection team that "PMS-Karvy has not derived any direct and indirect benefit out of the clients' funds and securities".

CONSIDERATION OF SUBMISSIONS AND FINDINGS

11. I have carefully perused the SCN along with the Enquiry Report, submissions made by the Noticee and all the documents/ evidence available on record. The issues that arise for consideration in the present case are:

11.1. Whether the Noticee has failed to appoint appropriately qualified or experienced Principal Officer thereby violating the provisions of Regulation 6(2)(c) of Portfolio Managers Regulations, 1993?

11.2. Whether the Noticee, by mentioning contrary provisions in its Disclosure Document, has violated the provisions of Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 and 9 of Schedule III of Portfolio Managers Regulations, 1993?

11.3. Whether the Noticee, by outsourcing core activities in Model Portfolio Management Agreement, has violated the provisions of Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 of Schedule III (Code of Conduct) of Portfolio Managers Regulations, 1993 and Clause 5 of SEBI Circular CIR/MIRSD/24/2011 dated December 15, 2011?

11.4. Whether the Noticee, by not maintaining uniformity in the condition of notice period mentioned in the model portfolio agreement regarding termination of agreement with clients, violated the provisions of Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 and 3 of Schedule III of Portfolio Managers Regulations, 1993?

11.5. Whether the Noticee has failed to provide certain details in Disclosure Document (By not providing details of penalties, pending litigation or proceedings, findings of inspection or investigations) thereby violating

provisions of Regulation 14(2)(a) of Portfolio Managers Regulations, 1993 read with sub-clause 4, Clause III of the Model Disclosure Document for Portfolio Management in Schedule V of Portfolio Managers Regulations, 1993 and Clause 3(b) of SEBI CIRCULAR Cir. /IMD/DF/16/2010 dated November 02, 2010?

11.6. Whether the Noticee, by keeping open positions in respect of allocation of purchases of securities effected in a day, violated provisions of Regulation 16(5) of Portfolio Managers Regulations, 1993?

11.7. Whether the Noticee by not rectifying the deficiencies in the auditors' report within two months of receipt of audit report, and failing to maintain proper trail of funds of the investors, which resulted in unreconciled bank balances, violated provisions of Regulation 15 (2) of Portfolio Managers Regulations, 1993 read with Clause 8 of Schedule IV of Portfolio Managers Regulations, 1993 and Regulation 22 of Portfolio Managers Regulations, 1993?

11.8. Whether the Noticee has failed to appoint appropriate compliance Officer thereby, violated provisions of Regulations 23A(1) of Portfolio Managers Regulations, 1993?

12. The aforesaid provisions are reproduced below –

SEBI (Portfolio Managers) Regulations, 1993

6. Consideration of application

(1) For considering the grant of certificate of registration to the applicant, the Board shall take into account all matters which it deems relevant to the activities relating to portfolio management.

(2) Without prejudice to the generality of the foregoing provisions, the Board shall consider whether-

(c) the principal officer of the applicant has either–

(i) a professional qualification in finance, law, accountancy or business management from a university or an institution recognized by the Central Government or any State Government or a foreign university; or

(ii) an experience of at least ten years in related activities in the securities market including in a portfolio manager, stock broker or as a fund manager.

(iii) a CFA charter from the CFA Institute.

9A. Conditions of registration.

(1) Any registration granted under regulation 8 shall be subject to the following conditions, namely:-

(c) it shall take adequate steps for redressal of grievances of the investors within one month of the date of the receipt of the complaint and keep the Board informed about the number, nature and other particulars of the complaints received.

13. Code of Conduct. *— Every portfolio manager shall abide by the Code of Conduct as specified in Schedule III.*

14. Contract with clients and disclosures.

(2) (a) The portfolio manager shall provide to the client, the Disclosure Document as specified in Schedule V, along with a certificate in Form C as specified in Schedule I, at least two days prior to entering into an agreement with the client as referred to in sub-regulation (1).

15. General responsibilities of a Portfolio Manager

(2) The portfolio manager shall act in a fiduciary capacity with regard to the client's funds.

(6) The portfolio manager shall ensure proper and timely handling of complaints from his clients and take appropriate action immediately.

16. Investment of clients' moneys and management of clients' portfolio of securities

(5) The portfolio manager shall, ordinarily purchase or sell securities separately for each client. However, in the event of aggregation of purchases or sales for economy of scale, inter se allocation shall be done on a pro rata basis and at weighted average price of the day's transactions. The portfolio manager shall not keep any open position in respect of allocation of sales or purchases effected in a day.

22. Report on steps taken on Auditor's report *— Every portfolio manager shall within two months from the date of the auditors report take steps to rectify the deficiencies, made out in the auditors report.*

23A. Appointment of compliance officer *—*

(1) Every portfolio manager shall appoint a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc., issued by the Board or the Central Government and for redressal of investors' grievances.

(2) The compliance officer shall immediately and independently report to the Board any non-compliance observed by him.

Schedule III of SEBI (Portfolio Managers) Regulations, 1993

[Regulation 13]

Code of conduct - portfolio manager

1. A portfolio manager shall, in the conduct of his business, observe high standards of integrity and fairness in all his dealings with his clients and other portfolio managers.

3. A portfolio manager shall render at all times high standards of service, exercise due diligence, ensure proper care and exercise independent professional

judgment. The portfolio manager shall either avoid any conflict of interest in his investment or disinvestment decision, or where any conflict of interest arises, ensure fair treatment to all his customers. He shall disclose to the clients, possible source of conflict of duties and interests, while providing unbiased services. A portfolio manager shall not place his interest above those of his clients.

9. A portfolio manager shall endeavor to –

(a) ensure that the investors are provided with true and adequate information without making any misguiding or exaggerated claims and are made aware of attendant risks before any investment decision is taken by them;

(b) render the best possible advice to the client having regard to the client's needs and the environment, and his own professional skills;

(c) ensure that all professional dealings are effected in a prompt, efficient and cost effective manner.

Schedule IV of SEBI (Portfolio Managers) Regulations, 1993

[Regulation 14]

Contents of agreement between the portfolio manager and his clients

8. Maintenance of Accounts-Maintenance of accounts separately in the name of the client as are necessary to account for the assets and any additions, income, receipts and disbursements in connection therewith, as provided under SEBI (Portfolio Managers) Regulations, 1993.

Schedule V of SEBI (Portfolio Managers) Regulations, 1993

[Regulation 14]

Disclosure document

MODEL DISCLOSURE DOCUMENT FOR PORTFOLIO MANAGEMENT

III. Contents of the Document

4) Penalties, pending litigation or proceedings, findings of inspection or investigations for which action may have been taken or initiated by any regulatory authority.

(i) All cases of penalties imposed by the Board or the directions issued by the Board under the Act or Rules or Regulations made thereunder.

(ii) The nature of the penalty/direction.

(iii) Penalties imposed for any economic offence and/ or for violation of any securities laws.

(iv) Any pending material litigation/legal proceedings against the portfolio manager/key personnel with separate disclosure regarding pending criminal cases, if any.

(v) Any deficiency in the systems and operations of the portfolio manager observed by the Board or any regulatory agency.

(vi) Any enquiry/ adjudication proceedings initiated by the Board against the portfolio manager or its directors, principal officer or employee or any person directly or indirectly connected with the portfolio manager or its directors, principal officer or employee, under the Act or Rules or Regulations made thereunder.

SEBI CIRCULAR CIR/MIRSD/24/2011 dated December 15, 2011

5. Activities that shall not be outsourced

The intermediaries desirous of outsourcing their activities shall not, however, outsource their core business activities and compliance functions. A few examples of core business activities may be – execution of orders and monitoring of trading activities of clients in case of stock brokers; dematerialisation of securities in case of depository participants; investment related activities in case of Mutual Funds and Portfolio Managers. Regarding Know Your Client (KYC) requirements, the intermediaries shall comply with the provisions of SEBI {KYC (Know Your Client) Registration Agency} Regulations, 2011 and Guidelines issued thereunder from time to time.

SEBI CIRCULAR Cir. /IMD/DF/16/2010 dated November 02, 2010

3. In order to bring about greater uniformity, clarity and transparency with regard to above issues, portfolio managers are advised to ensure the following;

b) To ensure compliance with regulation 14(2)(b)(iv) of SEBI (Portfolio Managers) Regulations, 1993, Portfolio Managers shall disclose the performance of portfolios grouped by investment category for the past three years as per the enclosed prescribed tabular format. Portfolio Managers shall also ensure that the disclosure document is given to all clients along with the account opening form at least two days in advance of signing of the agreement. In order to ensure that the clients have access to updated information about the portfolio manager, portfolio managers shall place the latest disclosure document on their website, wherever possible.

13. I will now proceed with my findings with respect to each of the alleged violation against the Noticee in the SCN dated June 30, 2022 along with Enquiry Report (hereinafter referred to as '**ER**): -

13.1. Whether the Noticee has failed to appoint appropriately qualified or experienced Principal Officer thereby violating the provisions of Regulation 6(2)(c) of Portfolio Managers Regulations, 1993, by not appointing a qualified or experienced Principal Officer?

13.1.1. Regulation 6(2)(c) of Portfolio Managers Regulations, 1993 requires the Principal Officer of a Portfolio Manager to have a professional qualification in finance, law, accountancy or business management from a university or an institution recognized by the Central Government or any State Government or a foreign university; or an experience of at least ten years in related activities in the securities market including in a portfolio manager, stock broker or as a fund manager; a CFA charter from the CFA Institute.

13.1.2. The DA has observed that Mr. Vikas Rajpal, who was appointed as Principal Officer of PMS-Karvy with effect from April 16, 2019 was

qualified as Bachelor of Engineering (B.E.) in Chemical Engineering (sourced from his LinkedIn profile) and was having experience of around 7.5 years as portfolio manager, investment advisor and fund manager (as submitted by the Noticee in its reply). He also had certification from NISM Series XV Certified Research Analyst. Hence, he was not adequately qualified or experienced for being designated/ appointed as Principal Officer, in terms of Regulation 6(2)(c) of Portfolio Managers Regulations, 1993.

13.1.3. The DA has recorded that the noticee has accepted that Mr. Vikas Rajpal was appointed as Principal Officer with effect from April 16, 2019, even though he was not appropriately qualified or experienced in terms of regulation 6(2)(c) of Portfolio Managers Regulations, 1993 prevailing at the time of appointment. Noticee has stated that in the absence of a qualified or experienced person available, Mr. Vikas Rajpal was given the position of Principal Officer in the interest of investors as a temporary arrangement, and that Mr. Sachin Mittal was appointed as Principal Officer in June, 2020 subsequently, who was duly qualified and experienced for the position. Noticee has further submitted that provisions of Portfolio Managers Regulations, 1993 in this regard were subsequently relaxed in SEBI (Portfolio Managers) Regulations, 2020, as it requires only minimum five years' experience for Principal officer in the securities market, whereas Portfolio Managers Regulations, 1993 requires 10 years of experience. As Mr. Vikas Rajpal had experience of around 7.5 years, there would not have been any breach of the regulations.

13.1.4. I note that Mr. Sachin Mittal, being appropriately qualified and experienced was appointed as a Principal Officer after a period of more than 13 months of appointment of Mr. Vikas Rajpal as Principal Officer,

which is quite long a duration to call it a temporary arrangement in the interest of investors. The Regulation specifies the qualification and experience required for a person to be appointed as a Principal Officer and the said statutory requirement has to be maintained and complied with by every SEBI registered PMS. Regulation does not give any exemption or relaxation for such temporary arrangement.

13.1.5. I note the submission of the noticee that the delay in appointment of the official as per the Regulations by a time period of more than 13 months has not compromised the needs or interests of the securities markets, nor does it mean that the clients were not handled efficiently. The noticee has therefore admitted the violation alleged against him and the finding by the DA. The fact that there was change in the requirement subsequently or that it did not impact/compromise the interest of investors/clients does not absolve the noticee from the violations established against him.

13.1.6. As recorded by the DA, the Regulation is categoric about the qualification and experience of the Principal Officer. This requirement is to ensure that PMS as a registered intermediary caters to the need of the investors and in the best interest of the securities market through a qualified and/ or experienced Principal Officer, who with adequate qualification and experience will be in the best position to handle the matters pertaining to the client of PMS efficiently.

13.1.7. In view of the above, I conclude that the Noticee, by not appointing the Principal Officer with adequate experience, has violated the provisions of regulation 6(2)(c) of Portfolio Managers Regulations, 1993.

13.2. Whether the Noticee, by mentioning contrary provisions in its Disclosure Document, has violated the provisions of Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 and 9 of Schedule III of Portfolio Managers Regulations, 1993?

13.2.1. The DA has mentioned that with regard to the placement fee, the disclosure document of PMS-Karvy, dated February 18, 2019 reads as under:

•*Section 10 – Nature of Expenses (clause (v) on Page 29) – "The Placement fee shall be deducted upfront from the Client's portfolio immediately on receiving the corpus from the client."*

•*Annexure A – Section II – Fees and Expenses pertaining to the portfolio strategies (Page 16) – "The placement fee so computed shall be completely recovered from client's portfolio within the first year of receiving corpus. The Placement fee shall be deducted from client's portfolio at end of each calendar quarter till completion of one year of receiving corpus*."

13.2.2. The DA has recorded that both the clauses are contrary as Section 10 mentions upfront deduction of fees, whereas the clause in Annexure A – Section II mentions that fees will be deducted at end of each calendar quarter till completion of one year of receiving corpus.

13.2.3. I note from the finding of the DA that the Disclosure Document contains the quantum and manner of payment of fees payable by the client for each activity, portfolio risks, complete disclosures in respect of transactions with related parties, the performance of the portfolio manager and the audited financial statements of the portfolio manager for the immediately preceding three years. Both the parties, the client and the portfolio manager, are bound by this document and the terms

and conditions mentioned therein. I agree that the Disclosure Document is a very crucial document while processing the application for portfolio management services.

13.2.4. The noticee in its reply dated November 23, 2022 before me has submitted that it was charging the placement fee from its clients upfront. Subsequently, during 2016-17, considering various representations from clients to deduct charges on a quarterly basis, in the interest of the clients, the noticee had changed the time period of charging placement fee in Annexure A- Section II of the disclosure documents. Since FY 2016-17, placement fees was being charged on a quarterly basis spread over one year uniformly to all clients (which was more advantageous and convenient to the clients), instead of upfront fees. It is noticee's submission that while acceding to the representations of the clients, the concomitant change was inadvertently not carried out at the relevant time in Section 10 of the disclosure document. It also stated that it is nobody's case that no placement fees has to be paid by the clients. The only issue arising from the alleged disclosures, was when to pay i.e. whether upfront or over a period of time over 1 year. The said inadvertent error, the noticee submitted, cannot be elevated to the status of "*negligence*" as sought to be done by the DA, especially as it was an innocuous lapse with no adverse consequence on the clients' interests.

13.2.5. The noticee has also stated that there is no adverse finding by the DA, that as a consequence of alleged contrary provisions in Disclosure Document, the noticee has compromised the interests or the rights of the investors or the interest of the securities markets in any manner. He also said that there are no client complaints in this regard. The violation, according to the noticee, can only be a technical, procedural and venial

violation, with no consequential impact on clients or the securities market in any manner.

13.2.6. The noticee, has not denied the violation. Rather, it states that the same was an inadvertent error. I reproduce the relevant provisions of law that are alleged to have been violated by the noticee. Regulation 13 of the said regulations mandate a portfolio manager to abide by the code of conduct specified in Schedule III therein. Clauses 1 and 9 of Schedule III instruct a portfolio manager to observe high standards of integrity and fairness in all its dealings, and that investors and clients are given true and adequate information, without any misguiding claims and ensure that all its professional dealings are effected in a prompt, efficient and cost effective manner. By recording contrary provisions in the Disclosure Document w.r.t the manner in which expenses are payable at the end of the clients, I am constrained to conclude that the noticee has failed to comply with Regulation 13 of the said Regulations read with Clauses 1 and 9 of Schedule III of Portfolio Managers Regulations, 1993. These two clauses are clearly misguiding the clients w.r.t the payment they have to make.

13.3. Whether the Noticee, by providing for outsourcing of core activities in the Model Portfolio Management Agreement, has violated the provisions of Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 of Schedule III (Code of Conduct) of Portfolio Managers Regulations, 1993 and Clause 5 of SEBI Circular CIR/MIRSD/24/2011 dated December 15, 2011?

13.3.1. Regulation 13 of of Portfolio Managers Regulations, 1993 clearly states that every portfolio manager must abide by the Code of Conduct as specified in Schedule III.

13.3.2. In terms of Clause 1 of the Code of Conduct – Portfolio Manager in Schedule III of Portfolio Managers Regulations, 1993, a portfolio manager shall, in the conduct of his business, observe high standards of integrity and fairness in all his dealings with his clients and other portfolio managers.

13.3.3. In terms of Clause 5 of SEBI CIRCULAR CIR/MIRSD/24/2011 dated December 15, 2011, the intermediaries desirous of outsourcing their activities shall not, however, outsource their core business activities and compliance functions.

13.3.4. The DA has observed that Clause 2.18 of the Model Portfolio Management Agreement states that *"For the purpose of discharging any of the duties, obligations and functions (whether under this agreement or under the above mentioned Letter of Authority), of the Portfolio Manager, the Client hereby empowers the Portfolio Manager to act through any of its officers, employees or representatives or other person specifically authorized by the Portfolio Manager and the Portfolio Manager is empowered to delegate the performance of its duties, discretions, obligations, any of powers and authorities here under to such sub-delegates and pay fee/ consultancy charges that may be charged to the client's account."*

13.3.5. The above clause includes outsourcing of core activities of the Noticee. By making such provision in the model agreement, it was alleged that the Noticee has not observed high standards of integrity and fairness in all its dealings with its clients and has violated the provisions of Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 of Schedule III (Code of Conduct) of Portfolio Managers

Regulations, 1993 and Clause 5 of SEBI Circular CIR/MIRSD/24/2011 dated December 15, 2011.

13.3.6. Noticee has submitted that they have not outsourced the core activities to anyone and the instant clause was inserted to delegate only the routine and incidental operational activities pertaining to investment decisions (viz. interacting with other intermediaries such as Brokers, AMC's etc on Client's behalf to facilitate the transactions in the portfolio, to provide for appointment of custodian, to seek best fund accounting services etc as and when required) so as to maintain speed and efficiency in operations.

13.3.7. The Noticee has also submitted that at all points of time, actual core activities, including, picking the stocks for investment, timing of the investment, price at which investments are to be made, quantum of investments to be made, etc. was exclusively decided by the Portfolio Manager.

13.3.8. The Noticee has also stated that inspection report of SEBI in this matter clearly states that core activities have not been outsourced as on date of inspection, which shows that the Noticee did not intend to misuse the clause.

13.3.9. The portfolio manager, before taking up an assignment of management of funds or portfolio of securities on behalf of the client, enters into an agreement in writing with the client, clearly defining the *inter se* relationship and setting out their mutual rights, liabilities and obligations relating to the management of funds or portfolio of securities, containing the details as specified in Schedule IV of the Portfolio Managers

Regulations, 1993. Hence, the document shall be clear and explicit in its wordings.

13.3.10. I find that Regulation does not allow PMS to outsource any of its core activities. While the Noticee did not outsource its core activities, yet the aforementioned clause in the Model Portfolio Management Agreement establishes that the Noticee had a provision in the said agreement to outsource any of its activities. Further, Noticee contended that such clause does not mention that it was intended to outsource daily and routine operational activities. It is observed that clause 2.18 in the said agreement allows the Noticee "*to delegate the performance of its duties, discretions, obligations, any of powers and authorities here under"* and this purports to outsource the core activities.

13.3.11. I find from the Inspection Report as well as Enquiry Report that the Noticee has not outsourced its core activities. Even though the language used in the said clause of the agreement gives it a very broad meaning which may include delegation of core activities carried out by the Noticee, the fact that the Noticee has, in execution of such provision, never delegated its core activities to any other person cannot be ignored. The Regulation clearly does not allow PMS to outsource any of its core activities. However, I find that the Noticee has not delegated its core activities to any delegatee and therefore, I would like to take a lenient view with respect to the said allegation and conclude that the violation of provisions of Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 of Schedule III (Code of Conduct) of Portfolio Managers Regulations, 1993 and Clause 5 of SEBI Circular CIR/MIRSD/24/2011 dated December 15, 2011 is not established against the Noticee.

13.4. Whether the Noticee, by not maintaining uniformity in the condition of notice period mentioned in the model portfolio agreement regarding termination of agreement with clients, violated the provisions of Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 and 3 of Schedule III of Portfolio Managers Regulations, 1993?

13.4.1. As per Clause 3 of Schedule III of Portfolio Managers Regulations, 1993, a portfolio manager shall render high standards of service, exercise due diligence and independent professional judgement. A portfolio manager shall ensure fair treatment to its clients and shall not place his interest above those of his clients.

13.4.2. The DA has observed that Clauses 12.4 and 12.5 of the Model Portfolio Management Agreement of the Noticee state as under:

Clause 12.4 – "The portfolio manager may at any time terminate this agreement by written notice of termination to the Client."

Clause 12.5 – "In addition to being entitled to terminate this Agreement under Clause 4, the Client may at any time terminate this Agreement by giving not less than 30 days prior written notice of termination to the Portfolio Manager"

13.4.3. From the above, it was observed that there is no uniformity in condition of notice period regarding termination of agreement. The Noticee has made provision for termination of client without specifying any time, which is alleged to be not in the interest of the clients and failure to maintain high standards of integrity and fairness on part of the Noticee in all its dealings with clients.

13.4.4. Clause 12.4 of the Model Portfolio Management Agreement of the Noticee allows the Noticee to terminate the agreement at any time by written notice of the same to the client. However, as per clause 12.5, the client may terminate the agreement by giving not less than 30 days prior written notice to the Noticee.

13.4.5. I note from the submission made by the Noticee that the Noticee had fairly accepted that there is lack of uniformity in Clauses 12.4 & 12.5 of the Agreement and that same was an inadvertent error and that Noticee has never terminated or suspended any client's account immediately, except in circumstances such as death of a client or the client being banned by SEBI.

13.4.6. In view of the above, I agree with the findings of DA that Noticee has violated the provisions of Regulation 13 of Portfolio Managers Regulations, 1993 read with Clauses 1 and 3 of Schedule III of Portfolio Managers Regulations, 1993.

13.5. Whether the Noticee has failed to provide certain details in Disclosure Document (By not providing details of penalties, pending litigation or proceedings, findings of inspection or investigations) thereby violating provisions of Regulation 14(2)(a) of Portfolio Managers Regulations, 1993 read with sub-clause 4, Clause III of the Model Disclosure Document for Portfolio Management in Schedule V of Portfolio Managers Regulations, 1993 and Clause 3(b) of SEBI CIRCULAR Cir. /IMD/DF/16/2010 dated November 02, 2010?

13.5.1. Regulation 14 (2)(a) of Portfolio Managers Regulations, 1993 clearly states that the portfolio manager must provide to the client, the Disclosure Document as specified in Schedule V, along with a certificate

in Form C as specified in Schedule I, at least two days prior to entering into an agreement with the client as referred to in sub-regulation (1).

13.5.2. In terms of Sub-Clause 4, Clause 3 of the Model Disclosure Document for Portfolio Management in Schedule V of Portfolio Managers Regulations, 1993, the Disclosure Document of a Portfolio Manager should contain details, as mentioned therein, of penalties, pending litigation or proceedings, findings of inspection or investigations for which action may have been taken or initiated by any regulatory authority. Clause 3(b) of SEBI CIRCULAR Cir. /IMD/DF/16/2010 dated November 02, 2010 specifically mentions to place the latest disclosure document on the website of the portfolio manager.

13.5.3. The DA has observed that the latest Risk Disclosure Document dated August 29, 2019, available on website of the Noticee, i.e. www.karvypms.com, contained 54 pages. Under Section 4 of the Disclosure Document – Penalties, Pending Litigation or Proceedings, Findings of Inspection or Investigations for which action may have been taken or initiated by any Regulatory Authority, 'Annexure B' was referred for this information. However, said 'Annexure B' was not found within the Disclosure Document on the website. It was, therefore, alleged that by not providing details of penalties, pending litigation or proceedings, findings of inspection or investigations for which action may have been taken or initiated by any regulatory authority, the Noticee has violated Regulation 14(2)(a) of Portfolio Managers Regulations, 1993 read with sub-clause 4, Clause III of the Model Disclosure Document for Portfolio Management in Schedule V of Portfolio Managers Regulations, 1993 and Clause 3(b) of SEBI CIRCULAR Cir. /IMD/DF/16/2010 dated November 02, 2010.

13.5.4. The Noticee has submitted that there was Annexure B of 54 pages which included all the details of penalties, pending litigation or proceedings, findings of inspection or investigations for which action may have been taken or initiated by any regulatory authority and the said information was transparently disclosed to all its clients, in hard copies.

13.5.5. I also note from the submission made by the Noticee that the details were not placed on their website and the Noticee has accepted the allegation and submitted that it was an inadvertent error, with no consequential impact.

13.5.6. Clause 3(b) of SEBI CIRCULAR Cir. /IMD/DF/16/2010 dated November 02, 2010 clearly requires the portfolio managers to place the latest disclosure document on their website. Even though the disclosure document was placed on Noticee's website, the Annexure 'B', which contained 54 pages of the details of penalties, pending litigation or proceedings, findings of inspection or investigations for which action may have been taken or initiated by any regulatory authority, was not present within the disclosure document, though the annexure forms part of this document. The said provisions have been made to bring transparency in the workings of a portfolio manager. However, the Noticee has not provided such details with respect to penalties, pending litigation or proceedings, etc.

13.5.7. In view of the above, I conclude that Noticee has violated provisions of Regulation 14(2)(a) of Portfolio Managers Regulations, 1993 read with sub-clause 4, Clause III of the Model Disclosure Document for Portfolio Management in Schedule V of Portfolio Managers Regulations, 1993 and Clause 3(b) of SEBI CIRCULAR Cir. /IMD/DF/16/2010 dated November 02, 2010.

13.6. Whether the Noticee, by keeping open positions in respect of allocation of purchases of securities effected in a day, violated provisions of Regulation 16(5) of Portfolio Managers Regulations, 1993?

13.6.1. Regulation 16 (5) of of Portfolio Managers Regulations, 1993 clearly states that the portfolio manager must not keep any open position in respect of allocation of sales or purchases effected in a day.

13.6.2. The DA has observed that on many instances, the Noticee kept open positions in respect of allocation of sales or purchases effected in a day from the transaction statement of the pool securities account of Noticee. The same has also been accepted by the Noticee in its response to inspection observations vide its email dated August 09, 2020. Hence, it was alleged that the Noticee has violated the provisions of Regulation 16(5) of Portfolio Managers Regulations, 1993.

13.6.3. The Noticee has submitted that the open positions were exceedingly insignificant i.e. 2 days from the entire one year which was purely unintentional and an error of inadvertence and also no complaints were received by their clients in this regard.

13.6.4. I note from the submission made by the Noticee that the Noticee has accepted the allegation and submitted that during inspection period of one year, there were only two days (i.e. July 23, 2018 and July 24, 2018) when the violation occurred, which was unintentional and inadvertent. I find from the Annexure 6 to the Show Cause Notice dated January 19, 2022 that the violation occurred on 7 days (i.e. May 08, 2018, May 14, 2018, July 06, 2018, July 23, 2018, July 24, 2018, July 27, 2018 and

December 03, 2018) and for more than 40 scrips. The said error on the part of the Noticee cannot be considered as insignificant as keeping open position and leveraging its position was not in the interest of investors and posed a risk to its clients.

13.6.5. In view of the above, I conclude that Noticee has violated provisions of Regulation 16(5) of Portfolio Managers Regulations, 1993.

13.7. Whether the Noticee by not rectifying the deficiencies made in the auditors' report within two months of receipt of audit report, and its failure to maintain proper trail of funds of the investors, which resulted in unreconciled bank balances, violated provisions of Regulation 15 (2) of Portfolio Managers Regulations, 1993 read with Clause 8 of Schedule IV of Portfolio Managers Regulations, 1993 and Regulation 22 of Portfolio Managers Regulations, 1993?

13.7.1. Regulation 15(2) of Portfolio Managers Regulations, 1993 mandates a portfolio manager to act in a fiduciary capacity with regard to client's funds. Regulation 22 of Portfolio Managers Regulations, 1993 requires a portfolio manager to take steps to rectify the deficiencies made out in the auditor's report, within two months from the date of such report. Clause 8 of Schedule IV of Portfolio Managers Regulations, 1993 requires a portfolio manager to maintain accounts of clients as are necessary to account for clients' assets, additions, disbursements, income and receipts.

13.7.2. The DA has observed that certain amounts were pending un-reconciled in the pool bank account of Noticee. The said observation was also mentioned in the Internal Audit Reports for the half years ended on September 30, 2018 and March 31, 2019, wherein, it was observed that

on review of bank book and bank reconciliation as on March 31, 2019, there were un-reconciled bank balances in non-pool account of 5 clients and in the pool accounts of 15 clients. It was also observed in the said reports that there were certain discrepancies in reconciliation of amounts due to the software 'Miles' used by the Noticee. The observation related to unreconciled balances has also been accepted by Noticee in its response to inspection observations vide its email dated August 09, 2020.

13.7.3. I note that the Noticee has accepted the allegation and submitted that the amounts/differences were minimal and involve insignificant amount vis-à-vis the total amounts handled by PMS-Karvy. That the differences and unreconciled items are due to operational reasons, viz. non-identification of individual clients to whom such balances pertained is the response given by the Noticee.

13.7.4. I also note from the submission of the Noticee that it was decided by them that amounts should be transferred *pro rata* to the accounts of all investors belonging to the particular schemes. However, the Noticee has stated that before their client could implement their decision, their bank account was frozen.

13.7.5. I note that the Regulation clearly states that there should not be unreconciled differences lying in the books for a long time, except for reasons beyond the control of a portfolio manager. Also, allegation pertains to corrective actions not being taken by the Noticee, when it was in Noticee's control to identify and settle the differences. The Noticee's submission that its bank accounts are frozen since December, 2020 is untenable, as the unreconciled balances pertain to financial year 2018-19 and the bank accounts were frozen after around 21 months of the end of the financial year and the inspection period.

13.7.6. In view of the above, I conclude that the Noticee has violated provisions of Regulation 15 (2) of Portfolio Managers Regulations, 1993 read with Clause 8 of Schedule IV of Portfolio Managers Regulations, 1993 and Regulation 22 of Portfolio Managers Regulations, 1993.

13.8. Whether the Noticee has failed to appoint appropriate compliance Officer and thereby violated provisions of Regulations 23A(1) of Portfolio Managers Regulations, 1993?

13.8.1. Regulation 23A (1) of Portfolio Managers Regulations, 1993 requires an applicant desirous of being registered with SEBI as a portfolio Manager must appoint a compliance officer who shall be responsible for monitoring the compliance of SEBI Act, 1992, the rules and regulations, notifications, guidelines, instructions, etc. and also for redressal of investor grievances.

13.8.2. The DA has observed that Mr. Vikas Rajpal, who was appointed as Principal Officer of PMS-Karvy with effect from April 16, 2019 was not appropriately qualified or experienced for being designated as Principal Officer.

13.8.3. I note that the Noticee has made the submission that many of their employees had resigned from PMS-Karvy, including the then Principal Officer Mr. Rupin Shah -who had resigned from the Company during 2018-2019. PMS-Karvy had, keeping the interest of investors in mind, identified and appointed an existing staff member Mr Vikas Rajpal as Principal Officer/Compliance Officer. The Noticee has submitted that during that time he was the only officer whose qualification and experience was close to the requirements of a Principal

Officer/Compliance officer, as prescribed by SEBI. Subsequently, in July 2020, PMS-Karvy had appointed Mr. Shankhadeep Nath as the Compliance Officer.

13.8.4. Although the Noticee has submitted that the violation is a technical one and has not affected/compromised the rights of investors or interest in secondary market, I note that the Noticee, by failing to appoint appropriate Compliance officer, has violated provisions of Regulations 23 A (1) of Portfolio Managers Regulations, 1993.

14. I note that SEBI has issued the SEBI (Portfolio Managers) Regulations, 2020 in supersession of the SEBI (Portfolio Managers) Regulations 1993, which stand repealed with effect from 16 January 2020. However, I also note that the following violations committed by the Noticee have taken place prior to the existence of SEBI (Portfolio Managers) Regulations, 2020 and therefore, by virtue of regulation 42 (2) (c) of SEBI (Portfolio Managers) Regulations, 2020 titled "Repeal and Savings", the said violations are governed by SEBI (Portfolio Managers) Regulations 1993 and relevant Circulars which are mentioned as under:

14.1. Regulation 6(2)(c) of Portfolio Managers Regulations, 1993,

14.2. Regulation 13 read with clauses 1, 3 and 9 of Schedule III (Code of conduct) of Portfolio Managers Regulations, 1993 and Clause 5 of SEBI Circular CIR/MIRSD/24/2011 dated December 15, 2011,

14.3. Regulation 14(2)(a) read with sub-clause 4, Clause III of the Model Disclosure Document for Portfolio Management in Schedule V of Portfolio Managers Regulations, 1993 and Clause 3(b) of SEBI Circular No. CIR/IMD/16/2020 dated November 02, 2010,

14.4. Regulation 16(5) of Portfolio Managers Regulations, 1993,

14.5. Regulation 15(2) read with clause 8 of Schedule IV and Regulation 22 of Portfolio Managers Regulations, 1993,

14.6. Regulations 23A (1) of Portfolio Managers Regulations, 1993.

15. While the Noticee has submitted in its reply that it is not having active operations since November, 2019 and it is in the process of surrendering its certificate of registration as portfolio manager, I find that the Noticee being a registered intermediary is required to comply with the various Circulars, Rules and Regulations in place during the tenure of its registration. The very purpose of the said provisions is to deter the wrong doing and promote ethical conduct in the securities market.

16. The Noticee has also made submission with respect to the doctrine of proportionality by citing certain decisions by Hon'ble Supreme Court and Hon'ble Securities Appellate Tribunal (hereinafter referred to as "SAT"). The Noticee in his reply has placed reliance on the orders of Hon'ble SAT in the following appeals wherein the Hon'ble SAT has observed that the purpose of carrying out an inspection is not punitive and the object is to make the intermediary comply with the procedural requirements and that minor discrepancies, irregularities are not culpable:

16.1. Excel Crop Care Ltd. v. CCI, (2017) 8 SCC 47

16.2. Coimbatore District Central Coop. Bank v. Employees Assn. [Coimbatore District Central Coop. Bank v. Employees Assn., (2007) 4 SCC 669]

16.3. UPSE Securities Limited vs. SEBI (Appeal No. 109 of 2011, date of order – July 25, 2011)

16.4. Religare Securities Limited vs. SEBI (Appeal No. 23 of 2011, date of order – June 16, 2011)

16.5. JHP Securities vs SEBI (SAT Appeal no 121 of 2012)

17. I note that in the aforesaid order relied upon by the Noticee, the Hon'ble SAT itself has added a caveat to the effect that SEBI is not precluded from taking action against a delinquent in case of serious lapses. From the preceding paragraphs, I note that the following multiple violations have been established against the Noticee, which cannot be dismissed as technical, procedural, and venial in nature:

17.1. Failed to appoint appropriately qualified or experienced Principal Officer.

17.2. By mentioning contrary provision in its Disclosure Document.

17.3. By not maintaining uniformity in the condition of notice period mentioned in the model portfolio agreement regarding termination of agreement with clients.

17.4. Failed to provide certain details in Disclosure Document (By not providing details of penalties, pending litigation or proceedings, findings of inspection or investigations).

17.5. By keeping open positions in respect of allocation of purchases of securities effected in a day.

17.6. By not rectifying the discrepancies in the auditor's report.

17.7. Failed to appoint appropriate Compliance Officer.

18. The Noticee has submitted that the violations established against the Noticee should be considered leniently. However, I note that high degree of diligence is expected from a registered portfolio manager. Further, the Noticee is a big player in the securities market. Under the facts and circumstances of the case, I find that the violations committed by the Noticee cannot be brushed aside as technical or venial. In view of the same, I note that the Noticee's reliance on the aforesaid judgments is misplaced.

19. Therefore, in view of the facts and circumstances, as brought out in the foregoing paragraphs and the violations as established above, the Noticee is liable for

action under Regulation 27 of the Intermediaries Regulations read with Section 12(3) of SEBI Act.

20. The Noticee has contended that violations are technical and had no impact whatsoever on their clients' interests in any manner. I find that there are multiple violations of the Portfolio Manager Regulations and the same have been established in the preceeding paragraphs. The said violations have even been admitted by the Noticee. I find merit in the findings of the DA in the ER as stated above. However, I find that suspension for a period of one month will suffice in the facts and circumstances of the case.

ORDER

21. In view of the violations as established, facts and circumstances of the case, I find that the instant enquiry proceedings initiated vide the SCN dated June 09, 2022 against the Noticee viz. Karvy Stock Broking Limited is a fit case for suspension of the certificate of registration as specified under Regulation 27 of the Intermediaries Regulations and Section 12(3) of the SEBI Act, 1992.

22. In view of the foregoing, I, in exercise of powers conferred under Section 19 of the Securities and Exchange Board of India Act, 1992 Regulation 27(5) of the Intermediaries Regulations read with Regulation 41 of the Portfolio Managers Regulations and Section 12(3) of the SEBI Act, 1992, hereby direct the suspension of certificate of registration of the Noticee, i.e., Karvy Stock Broking Limited [Registration No. INP00001512] for a period of one month.

23. This Order comes into force with immediate effect.

24. A copy of this order shall be served upon to the Noticee and the Recognized Stock Exchanges to ensure necessary compliance.

25. The Show cause notice dated June 30, 2022 issued to the Noticee, i.e., Karvy Stock Broking Limited is disposed of accordingly.

Place: Mumbai **DR. ANITHA ANOOP**

Date: November 30, 2022 **CHIEF GENERAL MANAGER**

SECURITIES AND EXCHANGE BOARD OF INDIA