

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:

Name of the Noticee	SEBI Registration No.
Edelweiss Broking Limited (Now known as Nuvama Wealth and Investment Limited)	INZ000005231

In the matter of alleged fraud involving physical shares and demat accounts of certain entities.

Background:

1. The present proceedings originate from the investigation conducted by the Securities and Exchange Board of India (hereinafter referred to as '**SEBI**'), pursuant to two news articles dated January 08, 2014, *inter alia*, alleging the dematerialization and selling of shares in dormant accounts using forged documents by certain entities during the period from September 14, 2009 till March 08, 2013 (hereinafter referred to as '**Investigation Period**'). SEBI's investigation revealed that shares of 14 listed companies were allegedly acquired in the name of 26 bogus and non-existing entities through transfer of allegedly stolen or counterfeit physical shares and the said shares were subsequently dematerialized in the accounts of these 26 bogus entities.
2. It was observed during the course of investigation that Edelweiss Broking Limited (hereinafter referred to as the "**the noticee/ EBL**"), a registered stock broker and a member of BSE Limited ('**BSE**') and National Stock Exchange of India Limited

(**'NSE'**), had allegedly failed to exercise due skill, care, diligence, professionalism and efficiency in the conduct of its business, in relation to the dealings of one of its clients, viz. Mr. Yatin Vasantrai Parekh (hereinafter referred to as **"Mr. Parekh/Client"**). It was observed during the investigation that the noticee had:

- a) failed to exercise due skill, care, diligence, professionalism and efficiency with respect to ascertaining the identity of Mr. Parekh, at the time of placing orders with the noticee, *via* telephone; and
- b) failed to report the dealings of Mr. Parekh, which were not commensurate with his annual income, as declared in the Know Your Customer form (hereinafter referred to as **"KYC"**) to Financial Intelligence Unit (hereinafter referred to as the **"FIU"**).

3. In view of the above, it was alleged that the noticee had violated the provisions of Clause A(2) of Code of Conduct as specified in Schedule II read with regulation 9(f) of the Securities and Exchange Board of India (Stock-Brokers) Regulations, 1992 (hereinafter referred to as the **"Broker Regulations"**).
4. Pursuant to conclusion of the investigation, SEBI appointed a Designated Authority (hereinafter referred to as **'the DA'**) to inquire into and to submit a report pertaining to the probable violation of Clause A(2) of Code of Conduct as specified in Schedule II read with regulation 9(f) of the Broker Regulations.
5. The DA, after conducting the enquiry, as specified under regulation 25 of the Securities and Exchange Board of India (Intermediaries) Regulations, 2008 (hereinafter referred to as the **'Intermediaries Regulations'**), submitted the Enquiry Report dated July 29, 2022 (hereinafter referred to as the **"Report"**). In the said Report, the DA has observed that the allegation that the noticee failed to exercise due skill, care, diligence, professionalism and efficiency on account of not seeking PAN details, etc., of its client, i.e., Mr. Parekh at the time of placing the orders does not stand established.

6. As regards the second allegation i.e., non-reporting of ‘suspicious transactions’ to FIU by the noticee, the DA has observed that the noticee, as per paras 8, 9 and 2.2 of the guidelines of the SEBI Circular ISD/CIR/RR/AML/1/06 dated January 18, 2006, read with para 4 sub-clause (c) of Suspicious Transactions Report Guidelines mentioned under para 6 of SEBI Circular ISD/CIR/RR/AML/2/06 dated March 20, 2006 and para 10 and para 13 of SEBI Master Circular CIR/ISD/AML/3/2010 dated December 31, 2010 (hereinafter referred to as “**SEBI PML Circulars**”), was under an obligation to report certain transactions of Mr. Parekh to FIU, which it failed to do. The DA has found that by not adhering to the ‘SEBI PML Circulars’, the noticee failed to exercise due care and diligence, professionalism in the conduct of its business. Accordingly, the DA has recommended that the Certificate of Registration of the noticee (bearing no. INZ000005231), as a broker, may be suspended for a period of three months. The relevant excerpt of the Report is produced hereunder:

“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 October 04, 2018 against the Noticee viz. Edelweiss Broking Limited is a fit case for recommending punitive action in the form of suspension under Regulation 26(1)(iii) of the Intermediaries Regulations read with Regulation 27(xv) of the Broker Regulations and Section 12(3) of the SEBI Act, 1992. Therefore, in terms of Regulation 26(1)(iii) of the Intermediaries Regulations, I recommend that the registration of the Noticee, i.e., Edelweiss Broking Limited [registration No. INZ000005231] as a broker be suspended for a period of three months”

7. Pursuant to submission of the Report, a Post Enquiry Show Cause notice dated October 6, 2022 (hereinafter referred to as the “**SCN**”) enclosing a copy of the Report therewith was issued to the noticee to show cause as to why the action, as recommended by the DA, including other appropriate directions, if any, in terms of regulation 27 of the Intermediaries Regulations should not be taken/ issued against the noticee.

8. The noticee, vide its letter dated October 31, 2022 filed its reply to the SCN and requested for an opportunity of personal hearing, which was accordingly granted to the noticee on January 17, 2023, through video conferencing.
9. On the scheduled date of hearing, Mr. Somasekhar Sundaresan, Advocate, Authorized Representative, along-with Mr. Prashant Mody, Designated Director of the noticee, appeared and made oral submissions in the matter. As requested, the noticee was provided with 10 days' time to file post hearing submissions in the matter, which it filed vide letter dated January 27, 2023.
10. The submissions made by the noticee in its reply / written submissions dated October 31, 2022, January 27, 2023 and the oral submissions made during the course of personal hearing are summarized hereunder:
 - i. The DA has come to the conclusion that the first allegation, i.e., dealer of the Noticee should have asked for further details such as PAN, etc., does not stand established and therefore the present SCN is only restricted to the second allegation, i.e., dealings of Mr. Parekh were not commensurate with his income level and the noticee failed to report the same to FIU;
 - ii. The noticee denies that it has failed to exercise due care, diligence, and professionalism in the conduct of its business. The noticee further denies that it has violated the provisions of Clause A(2) of the Code of Conduct of Schedule II of the Brokers Regulations, read with regulation 9(f) of the Broker Regulations and Clause 1.2 and 1.3 of the Code of Conduct of Schedule III read with regulation 16 of the Intermediaries Regulations;
 - iii. The transactions in Mr. Parekh's account were not suspicious transactions:
 - a) The allegation in the Enquiry Report is that the noticee failed to adhere to the SEBI PML Circulars by not reporting suspicious transactions in its client's account to FIU and thereby failed to exercise due care and diligence, professionalism in the conduct of its business. The said conclusion was arrived as the daily turnover of Mr. Parekh on a few instances was more

- than the income declared by Mr. Parekh in the KYC at the time of account opening with the noticee;
- b) The trades carried out by Mr. Parekh were not suspicious transactions as they were not disproportionate with his annual income. A person may have large number of valuable assets but little or no income. A broker is required to set trading limits based on the margin/ collateral placed by the client and beyond that the noticee has no obligation to carry out examination of the client's income. The Enquiry Report has not addressed the aforesaid submission;
 - c) The SCN issued by the DA does not state the provision which required the noticee to allow a client to trade on the basis of his income level and even the Enquiry Report has not addressed the same;
 - d) The shares of Global Securities credited in the account of Mr. Parekh were not acquired through the noticee. Further, the Enquiry Report does not allege that the said shares were dematerialized through the noticee or the account of Mr. Parekh was a bogus account and the noticee failed to report the bogus account. The said shares were transferred through depositories over which the noticee has no control. Since the shares were not purchased through the noticee but transferred in the account of Mr. Parekh, the same did not raise any suspicion;
 - e) The Enquiry Report alleges that Mr. Parekh sold 97, 500 shares worth ₹21,77,070 and therefore the daily turnover of Mr. Parekh was not commensurate with the annual income of Mr. Parekh. However, there is no allegation that the said shares were transferred to any of the bogus entities and as these were exchange trades, the noticee was anyways not aware of the counterparty of these sell transactions. There is nothing in the Enquiry Report to suggest that there was anything illegal about the sell transactions entered into by Mr. Parekh. The funds received from these transactions were received in the account of Mr. Parekh and not in the account of any of the bogus entities. Thus, the transactions were not in violation of any rules or regulations and there was no lack of any due care, skill, diligence or professionalism by the noticee;

- f) The Enquiry Report mentions four instances namely, March 30, 2010, March 31, 2010, January 5, 2011 and January 17, 2011 to allege that the daily trading turnover of Mr. Parekh was not commensurate with his annual income but on none of these days the trading turnover of Mr. Parekh has crossed the declared annual income;
 - g) While the exchange stipulates a limit of 8.5 times of the broker's base capital, the noticee adopted a conservative approach and provided only 5 times the trading limit of the income declared by the clients and since Mr. Parekh's trading turnover never breached the said limit, the noticee was not required to report the same to any authority including FIU or Income Tax department;
- iv. Noticee has not violated the SEBI PML Circulars:
- a) The Enquiry Report relies upon SEBI Circular dated January 18, 2006 read with SEBI Master Circular dated December 31, 2010 to allege that the noticee failed to report suspicious transactions to FIU;
 - b) The only material relied upon in the Enquiry Report to allege that the noticee ought to have reported the transactions of Mr. Parekh is that the daily turnover of the noticee was more than his declared annual income on for six transactions. It is not the case in the Enquiry Report that the trades on all the said six transactions were fraudulent and illegal and that the shares were traded illegally on the exchange. There is no finding in the Enquiry Report regarding the authenticity of the transactions or legality of the funds used by Mr. Parekh in carrying out the transactions. There is nothing on record to show that the trades of Mr. Parekh could have aroused any suspicion in the mind of the noticee or that the trades were not bona fide or had no economic rationale;
 - c) The reliance placed on the decision of the Hon'ble Securities Appellate Tribunal (hereinafter referred to as the "**SAT**") in the matter of **Marwadi Shares and Finance Limited vs. SEBI**¹ (hereinafter referred to as "**Marwadi case**") is misplaced as the facts of the present matter are

¹ Order dated July 26, 2012, Appeal No. 85 of 2011

different. In the said case, there were 197 transactions on 88 trading days which were in the nature of single self-trades that had an effect on the price of the scrip and were fictitious transactions. In the present matter, there is no allegation that the transactions were illegal or fraudulent;

- d) The reliance on the decision of the Hon'ble SAT in the matter of ***Madhukar Seth vs. SEBI***² is misplaced as the said case is about broker aiding and abetting a client to deal with a scrip which led to market manipulation and creating false market in the scrip. In the present matter, there is no finding that the transactions in the account of Mr. Parekh were irregular or that the noticee was in any manner involved in the purported scam. In any case, the above referred case does not relate to broker's obligation to look at the declared annual income in the KYC before every transaction and thus, is irrelevant;
 - e) The guidelines on Anti-Money Laundering Standards and Combating the Financing of Terrorism/ Obligations of Securities Market Intermediaries under the Prevention of Money Laundering Act, 2002 and Rules, issued by SEBI specify a list of suspicious transactions but the same does not cover monitoring of trades based on the income declared in the KYC;
 - f) Since there was no glaring disparity, the noticee was not required to report such transactions to FIU and therefore the noticee has not violated SEBI PML Circulars;
- v. Noticee has acted with due skill, care and diligence in the conduct of its business under the Broker Regulations;
- a) The noticee has taken all steps necessary, including carrying out KYC, following instructions of the client, collecting margins, etc., and has therefore acted in terms of the Code of Conduct of the Broker Regulations which requires a broker to '*act with due skill, care and diligence in the conduct of all his business*';

² Decided on September 2003, Appeal No. 46 of 2002

- b) The law regarding due diligence is duly settled and the Hon'ble SAT in the matter of **MG Capital Services Limited vs. SEBI**³ has held as under:

“It is not enough to say that the appellant had failed to exercise skill, due care and diligence in so far as transactions of Rishabh with appellant's sister concern namely FMS are concerned. We are of the view that either the Board should bring out clearly as to what a stock broker was supposed to do which it has failed to do and thus violated a laid down norm. Due diligence would imply such care and skill as a man of ordinary prudence would exercise under similar circumstances. The finding of due diligence is to be sustained by convincing preponderance of probabilities standard.”

- vi. There is no finding in the Enquiry Report that the noticee has any connection with the purported scam or that the noticee has dealt with the proceeds of the crime;
- vii. The noticee had no dealings with any of the 26 bogus/ non-existent entities, the said entities are not clients of the noticee, the noticee does not have any contractual relationship with such entities, the noticee has not received/ remitted any funds or securities from/ to any of the bogus entities and not even a single physical share of any of the 14 entities was dematerialized through the noticee;
- viii. Even if it is assumed that the noticee failed to carry out the due diligence, the punitive action recommended by the DA is disproportionate. Even in the Marwadi case, despite the volume of the trades and the serious nature of the fictitious transactions, SEBI had imposed a penalty of ₹25,000 for failure to report the suspicious transactions;
- ix. The daily turnover of Mr. Parekh never crossed the declared annual income in 4 out of 6 instances and there is nothing on record to suggest that these 4 instances involved proceeds of crime/ were made in circumstances of unusual

³ 2012 SCC OnLine SAT 119

or unjustified complexity/ had no economic rationale which are essential elements of suspicious transactions under the Prevention of Money-laundering (Maintenance of Records of the Nature and Value of Transactions, the Procedure and Manner of Maintaining and Time for Furnishing Information and Verification and Maintenance of Records of the Identity of the Clients of the Banking Companies, Financial Institutions and Intermediaries) Rules, 2005 (**'PML Rules'**);

- x. On remaining 2 instances, i.e., May 21, 2012 and May 24, 2012, Mr. Parekh traded in the shares of Global Securities Limited but the said shares were credited to Mr. Parekh's account through depository system and were neither purchased nor dematerialized through the noticee;
- xi. Since the transaction on the aforesaid 2 instances only pertained to sale of shares already available in the client's account, the noticee was not required to look at the declared annual income as shares can also be gifted, and value of such shares can be much higher than the declared income of the recipient;
- xii. The SCN issued by the DA, *inter alia*, raised two allegations, i.e., noticee's dealer should have asked for further details such as PAN, etc., to confirm the genuineness of the caller and the dealings of Mr. Parekh were not commensurate with his annual income which the noticee failed to report to FIU/ income Tax department/ other financial regulator. Basis above, the DA alleged that the noticee had violated Clause A(2) of the Code of Conduct of the Schedule II read with regulation 9(f) of the Broker Regulations and Clauses 1.2 and 1.3 of the Code of Conduct, Schedule III read with regulation 16 of the Intermediaries Regulations, by failing to act with due care and diligence in the conduct of its business;
- xiii. While first allegation was dropped in the Enquiry Report, as regard the second allegation, the DA has held by not adhering to the SEBI PML Circulars, the noticee has failed to exercised due care and diligence in the conduct of its

business. The noticee was never given an opportunity to deal with the allegation of violation of SEBI PML Circulars. Further, the penalty of suspension recommended by the DA is only on the basis of the said allegation and since no opportunity was accorded to the noticee to deal with the allegation, the DA could not have recommended the penalty;

- xiv. The DA has failed to explain how the allegation of violating SEBI PML Circulars would fall under the provisions of Code of Conduct under the Brokers Regulations;
- xv. Though the Enquiry Report alleges that the noticee has violated the provisions of Code of Conduct under the Broker Regulations and Intermediaries Regulations, it fails to point out the due diligence, the noticee ought to have carried out;
- xvi. The Enquiry Report fails to point out as to how the noticee could have formed an opinion that transactions in Mr. Parekh's account were suspicious transactions without carrying out any investigation when SEBI and EoW had to carry out an extensive investigation to develop a suspicion regarding the scrip of Global Securities;
- xvii. The transactions were carried out on exchange platform in compliance with the extant regulatory provisions;
- xviii. The Hon'ble Supreme Court, in the case of **SEBI vs. Kishore R. Ajmera**⁴ has observed that when there is no direct proof to indicate that the broker was guilty of violating the provisions of the Code of Conduct, "*The test would always be that what inferential process that a reasonable/ prudent man would adopt to arrive at a conclusion*" and when "*there is no other material to hold either lack of vigilance or bona fides on the part of the sub-broker so as to make respondent-broker liable. An irresistible or irreversible inference of negligence/*

⁴ [(2016) 6 SCC 368]

lack of due care etc., in our considered view, is not established even on proof of the primary facts alleged so as to make respondent-broker liable under the Conduct Regulations, 1992...”;

- xix. Only on the ground that the noticee ought to have formed an opinion that the alleged transactions were suspicious transactions, the recommendation of suspension of certificate of registration of the noticee for 3 months is excessive and disproportionate to the allegations against the noticee;
- xx. The scale of operations of the noticee has also increased multi-fold since the investigation period of 2009-2013 as the noticee’s registered client base in 2013 was 3 lakhs which has increased to around 9 lakhs in 2022. Similarly, the noticee had around 480 employees in 2013 which has increased to around 2000 employees across all offices;

Consideration of Issues and Findings:

- 11. Having carefully examined all the materials available on record viz. the Enquiry Report, the SCN, the reply, written submissions and the oral submissions put forth during the course of personal hearing, the allegations against the noticee can be categorized under two heads. The *first* allegation is that the noticee failed to exercise due skill, care, diligence, professionalism and efficiency with respect to ascertaining the identity of Mr. Parekh at the time of placing orders with the noticee *via* telephone, and the *second* allegation is that the noticee failed to exercise due diligence in reporting certain transactions of Mr. Parekh which were not commensurate with his declared annual income, to FIU.
- 12. As regards the *first* allegation, the DA in the report has observed that the aforesaid allegation does not stand established against the noticee. The noticee had submitted before the DA that the unique details of its clients such as client code, holding details, ledger balances, margin balances, etc., were sought before execution of orders and the contract notes were also duly sent to the registered

Email IDs of the clients. In my view, the allegations levelled in the show cause notice issued by the DA have to be seen in light of the diligence undertaken by the noticee. The show cause notice issued by the DA, *inter alia*, states that the noticee ought to have obtained further details such as PAN Card, before executing the orders. I find merit in the submission of the noticee that the noticee was already relying on unique parameters, the details of which are only likely to be available with the client. Further, as observed by the DA, none of the circulars issued by SEBI, required the noticee to seek PAN details of a client at the time of placing of orders *via* telephone. Considering the above, I agree with the observations of the DA that the noticee did not fail to exercise due skill, care, diligence, professionalism and efficiency in ascertaining the identity of Mr. Parekh.

13. With respect to the *second* allegation of non-reporting of '*suspicious transactions*', after taking into consideration the contents of the SCN and the written and oral submissions made by the noticee, the issues under consideration before me are as under:

- a) Whether the transactions entered into by Mr. Parekh fall within the purview of the term '*suspicious transactions*' as defined under rule 2(1)(g) of the PML Rules?
- b) Whether the noticee has violated the SEBI PML Circulars by not reporting the suspicious transactions to FIU?
- c) Whether the noticee has violated the Clause A(2) of Code of Conduct as specified in Schedule II read with regulation 9(f) of the Broker Regulations?

14. Before dealing with the issue at hand, I deem apposite to refer to the relevant provisions of law alleged to have been violated in the matter, extracts whereof are reproduced below:

"SEBI (Stock Brokers) Regulations, 1992:

Conditions of registration.

9. Any registration granted by the Board under regulation 6 shall be subject to the following conditions, namely,-

...

(f) he shall at all times abide by the Code of Conduct as specified in Schedule II; and

SCHEDULE II

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

CODE OF CONDUCT FOR STOCK BROKERS

[Regulation 9]

A. General.

(1) ...

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

Rule 2(1)(g) of the PML Rules

(g) *"Suspicious transaction" means a transaction referred to in clause (h), including an attempted transaction, whether or not made in cash, which to a person acting in good faith-*

(a) gives rise to a reasonable ground of suspicion that it may involve proceeds of an offence specified in the Schedule to the Act, regardless of the value involved; or

(b) appears to be made in circumstances of unusual or unjustified complexity; or

(c) appears to have no economic rationale or bona fide purpose; or

(d) gives rise to a reasonable ground of suspicion that it may involve financing of the activities relating to terrorism;

Explanation. - Transaction involving financing of the activities relating to terrorism includes transaction involving funds suspected to be linked or related to, or to be used for terrorism, terrorist acts or by a terrorist, terrorist organisation or those who finance or are attempting to finance terrorism

SEBI PML Circulars

A. SEBI Circular dated January 18, 2006

2.2 As per the provisions of the Act, every banking company, financial institution (which includes chit fund company, a co-operative bank, a housing finance institution and a non-banking financial company) and intermediary (which includes a stock-broker, sub-broker, share transfer agent, banker to an issue, trustee to a trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and any other intermediary associated with securities market and registered under section 12 of the Securities and Exchange Board of India Act, 1992) shall have to maintain a record of all the transactions; the nature and value of which has been prescribed in the Rules under the PMLA. Such transactions include:

- All cash transactions of the value of more than Rs 10 lacs or its equivalent in foreign currency.
- All series of cash transactions integrally connected to each other which have been valued below Rs 10 lakhs or its equivalent in foreign currency where such series of transactions take place within one calendar month.
- All suspicious transactions whether or not made in cash and including, inter-alia, credits or debits into from any non monetary account such as dmat account, security account maintained by the registered intermediary.

It may, however, be clarified that for the purpose of suspicious transactions reporting, apart from 'transactions integrally connected', 'transactions remotely connected or related' should also be considered.

8. Monitoring of transactions

8.1 Regular monitoring of transactions is vital for ensuring effectiveness of the Anti Money Laundering procedures. This is possible only if the intermediary has an understanding of the normal activity of the client so that they can identify the deviant transactions / activities.

8.2 Intermediary should pay special attention to all complex, unusually large transactions / patterns which appear to have no economic purpose. The intermediary may specify internal threshold limits for each class of client accounts and pay special attention to the transaction which exceeds these limits.

8.3 The intermediary should ensure a record of transaction is preserved and maintained in terms of section 12 of the PMLA 2002 and that transaction of suspicious nature or any other transaction notified under section 12 of the act is reported to the appropriate law authority. Suspicious transactions should also be regularly reported to the higher authorities / head of the department.

8.4 Further the compliance cell of the intermediary should randomly examine a selection of transaction undertaken by clients to comment on their nature i.e. whether they are in the suspicious transactions or not.

9. Suspicious Transaction Monitoring & Reporting

9.1 Intermediaries should ensure to take appropriate steps to enable suspicious transactions to be recognised and have appropriate procedures for reporting suspicious transactions. A list of circumstances which may be in the nature of suspicious transactions is given below. This list is only illustrative and whether a particular transaction is suspicious or not will depend upon the background, details of the transactions and other facts and circumstances:

- a) Clients whose identity verification seems difficult or clients appears not to cooperate
- b) Asset management services for clients where the source of the funds is not clear or not in keeping with clients apparent standing /business activity;
- c) Clients in high-risk jurisdictions or clients introduced by banks or affiliates or other clients based in high risk jurisdictions;
- d) Substantial increases in business without apparent cause;
- e) Unusually large cash deposits made by an individual or business;
- f) Clients transferring large sums of money to or from overseas locations with instructions for payment in cash;
- g) Transfer of investment proceeds to apparently unrelated third parties;
- h) Unusual transactions by CSCs and businesses undertaken by shell corporations, offshore banks /financial services, businesses reported to be in the nature of export-import of small items.

9.2 Any suspicion transaction should be immediately notified to the Money Laundering Control Officer or any other designated officer within the intermediary. The notification may be done in the form of a detailed report with specific reference to the clients, transactions and the nature /reason of suspicion. However, it should be ensured that there is continuity in dealing with the client as normal until told otherwise and the client should not be told of the report/suspicion. In exceptional circumstances, consent may not be given to continue to operate the account, and transactions may be suspended, in one or more jurisdictions concerned in the transaction, or other action taken.”

B. SEBI Circular Dated March 20, 2006

6. Reporting to Financial Intelligence Unit-India

In terms of the PMLA rules, intermediaries are required to report information relating to cash and suspicious transactions to the Director, Financial Intelligence Unit-India (FIU-IND) at the following address:

**Director, FIU-IND,
Financial Intelligence Unit-India,
6th Floor, Hotel Samrat,
Chanakyapuri,
New Delhi-110021.**

Intermediaries should carefully go through all the reporting requirements and formats enclosed with this circular. These requirements and formats are divided into two parts- Manual Formats and Electronic Formats. Details of these formats are given in the documents (Cash Transaction Report- version 1.0 and Suspicious Transactions Report version 1.0) which are also enclosed with this circular. These documents contain detailed guidelines on the compilation and manner/procedure of submission of the manual/electronic reports to FIU-IND. The related hardware and technical requirement for preparing reports in manual/electronic format, the related data files and data structures thereof are also detailed in these documents. Intermediaries, which are not in a position to immediately file electronic reports, may file manual reports to FIU-IND as per the formats prescribed. While detailed instructions for filing all types of reports are given in the instructions part of the related formats, intermediaries should adhere to the following:

- (a) The cash transaction report (CTR) (wherever applicable) for each month should be submitted to FIU-IND by 15th of the succeeding month.*
- (b) The Suspicious Transaction Report (STR) should be submitted within 7 days of arriving at a conclusion that any transaction, whether cash or non-cash, or a series of transactions integrally connected are of suspicious nature. The Principal Officer should record his reasons for treating any transaction or a series of transactions as suspicious. It should be ensured that there is no undue delay in arriving at such a conclusion.*
- (c) The Principal Officer will be responsible for timely submission of CTR and STR to FIU-IND;*
- (d) Utmost confidentiality should be maintained in filing of CTR and STR to FIU-IND. The reports may be transmitted by speed/registered post/fax at the notified address.*

Guideline 4 of the STR attached with the Circular

4. Suspicious Transaction Report

The Prevention of Money laundering Act, 2002 and the Rules notified thereunder require every intermediary to furnish details of suspicious transactions whether or not made in cash. Suspicious transaction means a transaction whether or not made in cash which, to a person acting in good faith

—

(a) gives rise to a reasonable ground of suspicion that it may involve the proceeds of crime; or

(b) appears to be made in circumstances of unusual or unjustified complexity; or

(c) appears to have no economic rationale or bonafide purpose.

C. SEBI Master Circular dated December 31, 2010

10. Suspicious Transaction Monitoring & Reporting

10.1 Intermediaries shall ensure that appropriate steps are taken to enable suspicious transactions to be recognized and have appropriate procedures for reporting suspicious transactions. While determining suspicious transactions, intermediaries shall be guided by the definition of a suspicious transaction contained in PML Rules as amended from time to time.

10.2 A list of circumstances which may be in the nature of suspicious transactions is given below. This list is only illustrative and whether a particular transaction is suspicious or not will depend upon the background, details of the transactions and other facts and circumstances:

a) Clients whose identity verification seems difficult or clients that appear not to cooperate

b) Asset management services for clients where the source of the funds is not clear or not in keeping with clients apparent standing /business activity;

c) Clients based in high risk jurisdictions;

d) Substantial increases in business without apparent cause;

e) Clients transferring large sums of money to or from overseas locations with instructions for payment in cash;

f) Attempted transfer of investment proceeds to apparently unrelated third parties;

g) Unusual transactions by CSCs and businesses undertaken by offshore banks/financial services, businesses reported to be in the nature of export- import of small items.

10.3 Any suspicious transaction shall be immediately notified to the Money Laundering Control Officer or any other designated officer within the intermediary. The notification may be done in the form of a detailed report with specific reference to the clients, transactions and the nature /reason of suspicion. However, it shall be ensured that there is continuity in dealing with the client as normal until told otherwise and the client shall not be told of the report/suspicion. In exceptional circumstances, consent may not be given to continue to operate the account, and transactions may be suspended, in one or more jurisdictions concerned in the transaction, or other action taken. The Principal Officer/Money Laundering Control Officer and other appropriate compliance, risk management and related staff members shall have timely access to client identification data and CDD information, transaction records and other relevant information.

13. Reporting to Financial Intelligence Unit-India

13.1 In terms of the PML Rules, intermediaries are required to report information relating to cash and suspicious transactions to the Director, Financial Intelligence Unit-India (FIU-IND) at the following address:

**Director, FIU-IND,
Financial Intelligence Unit-India,
6th Floor, Hotel Samrat, Chanakyapuri,
New Delhi-110021.**

Website: <http://fiuindia.gov.in>

13.2 Intermediaries shall carefully go through all the reporting requirements and formats enclosed with this circular. These requirements and formats are divided into two parts- Manual Formats and Electronic Formats. Details of these formats are given in the documents (Cash Transaction Report- version 1.0 and Suspicious Transactions Report version 1.0) which are also enclosed with this circular. These documents contain detailed directives on the

compilation and manner/procedure of submission of the manual/electronic reports to FIU-IND. The related hardware and technical requirement for preparing reports in manual/electronic format, the related data files and data structures thereof are also detailed in these documents. Intermediaries, which are not in a position to immediately file electronic reports, may file manual reports with FIU-IND as per the formats prescribed. While detailed instructions for filing all types of reports are given in the instructions part of the related formats, intermediaries shall adhere to the following:

(a) The Cash Transaction Report (CTR) (wherever applicable) for each month shall be submitted to FIU-IND by 15th of the succeeding month.

(b) The Suspicious Transaction Report (STR) shall be submitted within 7 days of arriving at a conclusion that any transaction, whether cash or non-cash, or a series of transactions integrally connected are of suspicious nature. The Principal Officer shall record his reasons for treating any transaction or a series of transactions as suspicious. It shall be ensured that there is no undue delay in arriving at such a conclusion.

(c) The Principal Officer will be responsible for timely submission of CTR and STR to FIU-IND;

(d) Utmost confidentiality shall be maintained in filing of CTR and STR to FIU-IND. The reports may be transmitted by speed/registered post/fax at the notified address.

(e) No nil reporting needs to be made to FIU-IND in case there are no cash/suspicious transactions to be reported.

15. I now proceed to examine the issues framed at para 13 above on merits in light of the submissions made by the noticee and other material available on record.

16. The noticee has submitted that it was never given an opportunity of dealing with the alleged violation of the SEBI PML Circulars before the DA as the same was never raised in the SCN issued by the DA or at the time of hearing before the DA. In this regard, I am of the view that the Post Enquiry SCN issued to the noticee contained all relevant material, including the Enquiry Report, which in turn included the reliance on the SEBI PML Circulars. Further, as noted from the records the noticee has filed its written submissions on the alleged violations of the SEBI PML Circulars

and also made oral submissions in respect of the said alleged violations during the course of personal hearing dated January 17, 2023. Therefore, in my opinion, the noticee has been provided with a just and fair opportunity to present its case and make arguments as regards the reliance upon the SEBI PML Circulars in the present proceedings. Further, I observe from the SCN issued by the DA that even though the SEBI PML Circulars have not been specifically mentioned by the DA, the SCN issued by the DA contains the allegation that the noticee has failed to report certain transactions to FIU and/ or other authorities. Accordingly, I find that the submission of the noticee in this regard is devoid of merit.

17. The *first* issue that needs to be addressed in the present proceedings is whether the transactions executed by client of the noticee, i.e., Mr. Parekh would fall within the purview of the term '*suspicious transactions*', and if the same is answered in affirmative, whether the noticee defaulted by not reporting the said transactions to FIU. In order to examine the impugned transactions on the aforesaid criteria for judging whether a transaction is a suspicious transaction, it is imperative that the impugned transactions along with relevant observations of the DA are reproduced. The relevant excerpt from the report is reproduced hereunder:

"24. I also note from the details of off market dealings of Parekh annexed to the Investigation Report that Parekh had sold 97,500 shares of Global Securities Ltd worth Rs. 21,77,070 on May 21, 2012 and May 24, 2012, the details of which are given as under:-

<i>Trade Date</i>	<i>Quantity of shares</i>	<i>Value of shares (₹)</i>
<i>21/05/2012</i>	<i>50,000</i>	<i>10,30,000</i>
<i>24/05/2012</i>	<i>45,700</i>	<i>11,47,070</i>

25. Thus, I note from the foregoing that Parekh's daily trading turnover was greater than his declared annual income as per the KYC forms. Therefore, I note that Parekh's daily trading turnover was not commensurate with his declared Annual Income. In its statement recorded on July 15, 2015, the

Noticee has admitted that it did not report the trading activity of Parekh to FIU or Income Tax Department (ITD). ...

...29. However, I note from the details of trading turnover submitted by the Noticee that on certain trading days, Parekh's trading turnover was almost equal to or greater than his declared annual income of Rs. 10 to 15 Lakhs. The details are as under:

S. No.	Trade Date	Daily Trading Turnover (₹)	Income Mentioned by Parekh in KYC (₹)
1	30/03/2010	8,44,971	10 to 15 Lakhs
2	31/03/2010	5,84,800	10 to 15 Lakhs
3	05/01/2011	14,30,951	10 to 15 Lakhs
4	17/01/2011	12,00,000	10 to 15 Lakhs
5	21/05/2012	20,32,440	10 to 15 Lakhs
6	24/05/2012	23,05,670	10 to 15 Lakhs

From the above table, I observe that Parekh had generated total trading turnover of Rs. 14,29,771 on March 30, 2010 and March 31, 2010. Thereafter, Parekh further generated trading turnover of Rs. 14,30,951 on January 05, 2011, Rs. 12,00,000 on January 17, 2011. I further note that Parekh had generated trading turnover of Rs. 20,32,440 on May 21, 2012 and Rs. 23,05,670 on May 24, 2012. It clearly shows that the value of each of these daily transactions were nearly as much as or exceeded his declared annual income. Therefore, I do not accept the aforesaid contentions of Noticee."

The DA has further observed in para 31 of the report that "... I further note that, as per the SEBI PML Circulars, the reporting obligation is triggered at the very threshold of suspicion and does not require any conclusive proof of an illegal transaction. I note that given the fact that these transactions were not

commensurate with the income of Parekh, the said transactions give rise to a reasonable suspicion that Parekh may not be trading with a bona fide purpose and he may be acting as a front/conduit for somebody else, and therefore Parekh's aforesaid transactions amounted to suspicious transactions in terms of the SEBI PML Circulars and PML Rules and Noticee was under a stringent obligation to report such suspicious transactions in its client accounts to FIU-IND in terms of the SEBI PML Circulars. However, Noticee admittedly failed to do so. Thus, I find no merit in the contentions of the Noticee that it had acted with due diligence with respect to the transactions of Parekh and that there was no reason to report Parekh's transactions to the FIU-IND."

18. On perusal of the aforesaid observations of the DA, it is noted that the noticee is alleged to have not reported transactions entered into by Mr. Parekh on six days where the trading turnover of Mr. Parekh was not commensurate with his annual income, to FIU. It is observed in the report that, on these six instances, the trading turnover of Mr. Parekh was not commensurate with his annual income, as declared in the KYC records and this alone, as observed by the DA, should have alerted the noticee that the transactions entered into by Mr. Parekh may not have a bonafide purpose and, therefore, amounted to suspicious transactions. The relevant transactions are tabulated below for ready reference;

Table No. 1

S. No.	Trade Date	Daily Trading Turnover (₹)	Income Mentioned by Mr. Parekh in KYC (₹)
1	30/03/2010	8,44,971	10 to 15 Lakhs
2	31/03/2010	5,84,800	10 to 15 Lakhs
3	05/01/2011	14,30,951	10 to 15 Lakhs
4	17/01/2011	12,00,000	10 to 15 Lakhs
5	21/05/2012	20,32,440	10 to 15 Lakhs
6	24/05/2012	23,05,670	10 to 15 Lakhs

19. On a perusal of the above table, it is observed that on four out of six instances (Serial no.1-4), the daily trading turnover of Mr. Parekh was in the range of his

annual income. For the remaining two instances (at Serial no. 5 and 6), the daily trading turnover of Mr. Parekh was more than his declared annual income. As regards the said two transactions, I note from the observations of the DA that the trading turnover includes the turnover generated from sale of shares obtained by Mr. Parekh through off market transactions also. Out of the client's total trading turnover of ₹20.30 lakhs generated on May 21, 2012, the turnover from sale of shares obtained through off market transactions was ₹10.30 lakhs and on May 24, 2012, out of a total trading turnover of ₹23.05 lakhs, the turnover from sale of shares obtained through off market transactions was ₹11.47 lakhs.

20. The finding against the noticee in the Report that the aforesaid transactions were suspicious in terms of the PML Rules is based on the fact that the transactions entered into by Mr. Parekh were not commensurate with his declared annual income and the same should have aroused reasonable suspicion that Mr. Parekh may not be trading with a *bona fide* purpose and might be acting as a front/ conduit for somebody else. Accordingly, as per the findings of the DA, the noticee should have reported the said transactions to FIU as per the SEBI PML Circulars. This is the crux of the allegation against the noticee.

21. The noticee in its defence, has argued, that on four instances, the trading turnover of the client did not cross the declared annual income and further there is nothing in the Report or the SCN issued by the DA to indicate that these transactions involved proceeds of crime/ were made in circumstances of unusual or unjustified complexity/ had no economic rationale or bonafide purpose. In my view, such a defence does not stand when one analyzes these transactions in light of the definition of the term '*suspicious transactions*' under PML Rules. It must be kept in mind that the threshold for '*suspicion*' would be much below the threshold for a *full-fledged proof*. There need not be any conclusive evidence on record for a broker to suspect that the transactions of its clients suffered from one or more attributes of '*suspicious transactions*' as defined under PML Rules (reproduced at para 14 of this order). The legal obligation in the present case involved reporting of transactions to FIU if they appeared to be in the nature of such '*suspicious transactions*'. In the

present matter, the trading turnover of Mr. Parekh was not proportionate to his annual income and this alone should have alerted the noticee and should have aroused reasonable suspicion in the mind of the broker about the purpose of such transactions. The noticee has submitted in its reply dated October 31, 2022 that a person may have large number of assets but little or no income and therefore income cannot be a criterion for setting up trading limits. In this regard, I am of the view that it is not the case of the noticee that despite the daily trading turnover of Mr. Parekh being not commensurate with his declared annual income, the noticee had no reason to suspect the impugned transactions. The noticee has not argued that after finding the transactions to be suspicious, it had scrutinized the impugned transactions and looked into factors, such as, assets of Mr. Parekh and reached the conclusion that the impugned transactions were clear of any suspicion.

22. As regard the remaining two transactions, the noticee has submitted that the said transactions relate to sale of shares of Global Securities Limited and such shares were received in the account of Mr. Parekh through off-market transactions. As noted above, on May 21 and May 24, 2012 the total trading turnover of Mr. Parekh was ₹20.32 lakhs and ₹23.05 lakhs, respectively. Out of the said amounts, as noted in the Report, the sale turnover was ₹10.30 lakhs and ₹11.47 lakhs on May 21 and May 24, 2012. The said sell transactions pertained to sale of shares which were received by Mr. Parekh through off market transactions wherein the noticee has claimed that it had no involvement or notice of receipt of shares. For the sake of argument, even if the said sale turnover is not included in the total trading turnover of Mr. Parekh, the remaining daily trading turnover would still have been around ₹10.00 lakhs and ₹11.00 lakhs on May 21 and May 24, 2012, which would still have been just about equivalent to the annual income of Mr. Parekh. Therefore, it cannot be denied that the trading turnover was not commensurate with the declared annual income of Mr. Parekh. Thus, even after taking into account the value of shares received through off market transactions, the above mentioned transactions of Mr. Parekh remain 'not commensurate' with his annual income.

23. On the basis of available details of the transactions as discussed above, it might not have been reasonable to suspect that the transactions had been done in circumstances of unusual or unjustified complexity or involved the proceeds of an offence specified in the schedule of Prevention of Money-laundering Act, 2002 or involved financing of the activities relating to terrorism, but the disproportionate nature (in terms of value) of such transactions should have been enough to arouse suspicion about the bona fide purpose of such transactions. In this regard, I also note that the various SEBI PML Circulars discussed above have given illustrations of circumstances (which are not exhaustive), which would show that the transaction in question were 'suspicious' including 'where the source of funds is not clear or not in keeping with clients apparent standing /business activity'. In my view, the circulars explain with reasonable clarity as to when transactions can be treated as suspicious transactions.

24. Having found that the trading turnover of Mr. Parekh was not commensurate with his annual income and the same should have aroused a suspicion in the mind of the noticee and it should have reported the transactions to FIU, I answer the issues framed at Para 13(a) and (b) above in the affirmative. As observed by the Hon'ble SAT in the matter of **MG Capital Services Limited Vs. Securities and Exchange Board of India**⁵, cited by the noticee, '*...Due diligence would imply such care and skill as a man of ordinary prudence would exercise under similar circumstances.*' It is clear that the circumstances under which Mr. Parekh executed his transactions would have led any person of ordinary prudence to exercise care and diligence to report the transactions as suspicious in accordance with law. Since it is established that the noticee has violated the SEBI PML Circulars, I also answer the issue framed at para 13(c) in the affirmative to the extent that by violating the SEBI PML Circulars due to non-reporting of suspicious transactions to FIU, the noticee has also violated Clause A(2) of the Code of Conduct as specified in Schedule II read with regulation 9(f) of the Broker Regulations which requires the noticee to exercise due skill, care and diligence in the conduct of all its business.

⁵ 2012 SCC OnLine SAT 119

25. At this juncture, I consider it necessary to compare the facts of the present matter with the facts of the *Marwadi* case (distinguished by the noticee in its reply) to put things in a better perspective. The *Marwadi* case, *inter alia*, was in respect of execution of 200 trades, out of which 197 were self-trades. The Hon'ble SAT had therein held that 197 trades is not a small number and self-trades, by their very nature, are fictitious and had accordingly held the noticee therein, liable for non-reporting of suspicious transactions. The number of trades involved in the present matter before me is comparatively low and the allegations pertain only to six instances, executed in the years 2010-2012, wherein the annual income of Mr. Parekh was not commensurate with his annual income.

26. Having held that the noticee ought to have reported the transactions to FIU, I also deem it important to note down certain mitigating factors in the present matter in order to arrive at directions which are proportionate to the violations committed by the noticee. As noted above, the mis-match between the annual income and the trading turnover of Mr. Parekh, in the absence of any other evidence, is not glaring. Further, when the specific facts of the present case are placed against the case of *Marwadi* case, which has been relied upon by the DA, it is seen that the impugned instances are limited in number. In the present matter, there was a mismatch between the annual income of Mr. Parekh and his trading turnover and the noticee should have abided by the reporting obligations, which it failed to do. However, since only a small number of transactions are under consideration coupled with the fact that the trades were executed in 2010-12, I am of the view that a three months' suspension at this point of time would not be commensurate with the violation committed by the noticee. I, therefore, disagree with the quantum of punishment recommended by the DA and hold that issuance of regulatory censure to the noticee would be reasonable and would meet the ends of justice in the instant case.

Order

27. I, in exercise of the powers conferred upon me under Section 12(3) and Section 19 of the SEBI Act, 1992 read with Regulation 27(5) of the Intermediaries regulations,

hereby warn the noticee to be careful and diligent in the conduct of all its business, including recognizing and reporting suspicious transactions.

Sd/-

DATE: JUNE 20, 2023
PLACE: MUMBAI

ANAND R. BAIWAR
EXECUTIVE DIRECTOR
SECURITIES AND EXCHANGE BOARD OF INDIA