

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA
ORDER

Under Sections 11(1), 11B and 11D of the Securities and Exchange Board of India Act, 1992, read with the Securities and Exchange Board of India (Investment Advisers) Regulations, 2013 against -

1. CapitalVia Global Research Limited. (PAN: AADCC5782H, SEBI Registration No.INA200001512); and
Its Directors viz.
2. Mr. Kiran Ravindra Kumar Choudhary(PAN: AAEPK1536D),
3. Mr. Rohit Gadia (PAN: AGXPG1899A); and
4. Mr. Anshul Mansingka (PAN: AGRPM3025A).

Hearing before G Mahalingam, Whole Time Member, SEBI

Appearances

For noticees:

Mr. Rohit Gadia, CEO
Mr. Prem Prakash, CBO
Mr. Aniruddh Gokhale, Advisor Legal
Mr. Lokesh Dubey, Compliance Officer

For SEBI:

Mr. Naveen Sharma, Deputy General Manager
Mr. T. Venkateshwarlu, Assistant General Manager
Ms. Jayeeta Ray, Assistant General Manager
Ms. Amruta Sadguru Naik, Manager

BACKGROUND

1. CapitalVia Global Research Limited ("**CapitalVia**") registered as an Investment Adviser ("**IA**") under the Securities and Exchange Board of India (Investment Advisers) Regulations, 2013 (hereinafter referred to as the "**IA Regulations**") with effect from April 10, 2014 for a period of five years. CapitalVia has its registered office at 99, 1st Floor, Surya Complex, R.V. Road,

Basavangudi, Bangalore, Karnataka and its principal place of business at 903, B-1, 9th Floor, NRK Business Park, Scheme No.54, P-U-4, Indore-452010, Madhya Pradesh.

2. Pursuant to complaints received against CapitalVia, an inspection (hereinafter referred to as "**the Inspection**") was conducted by the Securities and Exchange Board of India (SEBI) on the second and third day of July, 2015 at the Indore office of CapitalVia. (One such complaint inter alia, alleged that "*CapitalVia charged a fee of Rs.25, 00,000/- for their services rendered wherein they promised an assured return of 10%.*"). The inspection revealed certain violations and non-compliances with the provisions of the IA Regulations. SEBI vide letter dated October 15, 2015 forwarded the Inspection report to CapitalVia and sought comments/explanations on the findings therein. Based on the response of CapitalVia, an interim order-cum-show cause notice dated November 11, 2016 (hereinafter referred to as "**the Interim order**") was passed against CapitalVia and its above named directors(collectively referred to as "**the Noticees**"), wherein the following directions were issued -

" ...

i. not to solicit or undertake any fresh advisory business with immediate effect till further directions.

*ii. to redress the grievances received against CapitalVia and to comply with all the provisions of IA regulations and submit a compliance report to SEBI within **three (3)** months from the date of receipt of this order.*

This Order shall be treated as a show cause notice and CapitalVia and its Directors viz: Mr. Kiran Ravindra Kumar Choudhary, Mr. Rohit Gadia, and Mr. Anshul Mansingka may show cause as to, why appropriate directions under the SEBI Act, 1992 and relevant SEBI Rules/Regulations including directions prohibiting them from buying, selling or otherwise dealing in securities market, either directly or indirectly, in any manner whatsoever, should not be issued against them. "

Against the aforesaid directions, CapitalVia filed Appeal No. 445/2016 before the Securities Appellate Tribunal (hereinafter referred to as "**SAT**"). The Hon'ble SAT vide order dated January 05, 2017 (hereinafter referred to as "**SAT order**") , held that since hearing had been fixed on 16th January, 2017, SEBI is directed to hear the appellant on 16th January, 2017 and pass an order by 20th January, 2017 and communicate the same to the appellant on 20th January, 2017 itself.

3. CapitalVia had filed its written reply to the Interim order vide letter dated December 12, 2016 (hereinafter referred to as "**Reply**"). including 13 Annexures each of which have been perused in detail. Further an opportunity of personal hearing was granted to the Noticees on January 16, 2017 (hereinafter referred to as "**the Hearing**"), when its representatives appeared and they were heard at length.

HEARING

4. Before getting into the issues that merit a careful adjudication, I would like to record the Noticee's oral submissions and my observations thereon wherever necessary:

(a) The entity is one of the first entrants in the field of Investment advisers at Indore with an employee strength of over 750. Capitalvia has a number of qualified experts/professionals to cater to the requirements of their clients including Chartered Market Technicians (CMTs) who are experts at technical analysis of market price movements. The CMTs are skilled professionals and their salary packages are market linked. CapitalVia has specialised departments to monitor marketing calls made to their clients by the staff in marketing division and they maintain distance from the risk profiling division. The average corpus per client is `30 lakh and they have a clientele of 3450 approximately. In short, the representatives submitted that it is a huge establishment and have been in the field from 2007-08 onwards.

(b) CapitalVia when asked specifically whether SEBI's directions restraining them from soliciting any fresh business were disclosed on its website, admitted that it has not been done so far. Further, they informed that the uninformed clients who were transferring funds on-line were informed through phone calls about the regulator's directions and the amounts were being duly refunded to those clients subsequently.

(c) Further, during the Hearing, when pointed queries were raised about the disproportionately high fees levied by them leading to creation of unrealistic expectations of return on the part of HNI clients, the representatives submitted that the Regulations do not provide a framework for calibration of the reasonableness of the fee levied. When questioned about the refund of the advisory fee which amounted to ` 24,59,856/- to one complainant, it was submitted that the amount was towards fee collected for three years and upon receipt of the complaint, they realised that it was "not the best case" and decided to refund. Capital Via further submitted that approximately ` 34 lakh was taken from another client for 3 years and the client corpus was ` 1 crore.

(d) During the Hearing, the representatives submitted that in general an investor/customer starts with basic products and gradually upgrades himself to the more complex ones. As regards risk profiling of the clients, Capital Via laid emphasis on its submission that its advice was based on historical chart analysis of price movements and this was suited for intra-day trading. By implication, it was indicated that intra-day trading being a less riskier approach did not require a systematic risk profiling process. Further, the representatives had no effective submissions with respect to the proof of communications sent to clients about their risk profile and other assessments and advices.

(e) When the representatives of CapitalVia were specifically asked as to why 'Investment Adviser' is not displayed as a part of their name, they justified saying that it would not be in the interest of their brand value without elaborating how.

(f) As far as the unsupported projections in the website are concerned, especially with respect to their activities in US and Singapore, it was submitted that these are for generating leads in the digital space and not intended to misrepresent.

(g) On KYC compliance, the representatives explained that there were initially no circulars of KYC applicable to IAs. From SEBI's side, it was pointed out that SEBI's letter dated May 19, 2014 communicating the grant of Certificate of Registration contained the specific condition that they should comply with SEBI(KYC Registration Agency) Regulations, 2011, and the same was not disputed by them.

(h) As far as the SEBI Complaints Redress System (SCORES) complaints relating to non-redressal of investor complaints are concerned, the entities stated that no pending complaints are there. Further, CapitalVia highlighted certain problems that are faced regarding the SCORES platform, particularly regarding the timeline within which complaints are received and closed. Since the issue does not have any direct bearing on the allegations/charges against CapitalVia, the same are not taken up for deliberation in this order.

(i) Also during the Hearing and in the Written Submissions made pursuant to Hearing, CapitalVia complained that their mails to SEBI did not elicit any response. I have perused the enclosed emails, and find that response was sent by SEBI Head Office at

Mumbai. It is also pertinent that in the email sent from CapitalVia to SEBI Head Office, they have sought a meeting to update SEBI regarding "corrective measures" taken internally thus further indicating and reiterating their admission that breach of regulatory provisions had, in fact, taken place. In this context, the Written Submissions also contain a statement that reads as follows:

"That, the CapitalVia had submitted its preliminary reply to the observations made by inspecting team and thereafter complied with all the obligations and responsibilities as required under Chapter III of the Regulations, 2013 and become fully compliant intermediary."

5. Pursuant to the Hearing, CapitalVia, vide an email, sent written submissions (hereinafter referred to as "**the written submissions**") reiterating the oral submissions made on the date of the Hearing. The said email was received on January 17, 2017 at 11.20 PM. The submissions included 9 Annexures, all of which have been carefully perused. The relevant points arising out of the written submissions and the annexures are separately discussed under each issue. However one broad observation is noted at this stage. CapitalVia has submitted Internal Audit Reports for three quarters i.e. from April, 2016 to December, 2016 conducted by one Fadnis & Gupte, Chartered Accountants, as per the scope of audit provided to them by CapitalVia. The Audit reports basically certify that certain compliances are in order. The Audit reports are at best cursory and do not provide details of the steps taken by CapitalVia to ensure compliance with IA Regulations. Hence, I am unable to consider these reports as valid proof of due compliance of the IA Regulations.

SCOPE AND OBJECT OF IA REGULATIONS:

6. It is relevant to appreciate the role of an Investment Adviser as contemplated under the IA Regulations in order to actually ascertain and assess the scope of breaches and its impact on the securities market on a holistic basis. The object of the IA Regulations, inter alia, was to lay down a framework for independent financial advisers which was absent till 2013 and to address the conflict of interest arising due to the dual role (advisory and sale) played by the distributors of financial products. Investment Advisors perform a pivotal role in the securities market of securing investor confidence in the integrity of the markets. This stems directly from the quality of advice provided to the investors which has to be honest and unbiased without being, in any way, swayed by short term profit motives. In addition to the statutory mandate under section 12 of the SEBI Act, 1992 to get registered, the regulation of investment advisory activity is necessary to avoid unscrupulous advisory business wherein investors could be misguided towards making investments in the securities market without providing them with an honest assessment of risks involved. There is thus a need to ensure discipline and transparency in this field of intermediation business in the securities market to protect the interest of the investors.

7. Investment advisers are understood to be persons who, for consideration, render advice relating to investment in securities or a portfolio of securities. Advice given as incidental to other primary activity are exempt from the purview of registered investment advisers. By definition therefore, the primary role of an investment adviser is to render, in good faith, advice that is suitable for investors. Consequently, the role of an investment adviser revolves around how accurately the risk assessment/profiling of a client is done, and how suitable is the advice rendered to the clients' risk profile and more importantly, the continuous channel of communication that an IA establishes with the clients to strengthen investor confidence. Prospective clients who approach investment advisers do so because their ability to evaluate the

complexities of the securities market may be inadequate, or because confidence in the investment will be enhanced by the advice of an informed professional. In any case, the high level of trust that the client/investor reposes in the adviser is the fulcrum on which the entire edifice of IA profession is predicated upon. The framework of the SEBI (Investment Advisers) Regulations, 2013 (hereinafter referred to as "**IA Regulations**") is structured towards protecting this trust, in addition to ensuring integrity of the securities market. The scheme of the IA Regulations makes it clear that besides laying down the registration requirements, and capital adequacy requirement, it elaborates on the general obligations and responsibilities in detail and step-wise risk profiling processes and how the advice should be methodically arrived at with respect to each client taking into consideration the clients' financials and investment objectives etc. The assessment of suitability of a product to a particular client, the necessity for all disclosures to be in place about the investment adviser itself and the pecuniary connections with the products as well as its affiliations to other entities associated with the securities market are all aimed at ruling out a potential conflict of interest. The success of the regulatory framework lies in the implementation of the same by the registered Investment advisers imbibing the spirit of the Regulations coupled with timely inspections conducted by the regulator.

SUMMARY OF ALLEGATIONS

8. The Interim order had listed 12 charges/allegations against the Noticees. For the purpose of this order, I am of the view that related issues/allegations can be taken up together for effective consideration. Accordingly I list the charges/allegations that arise from the Interim order as follows:

- I. Risk Profiling of clients and Suitability of Advice to Clients/Investors
- II. Non-compliance with fiduciary obligations and responsibilities and not acting with due skill, care & diligence
- III. False and Inadequate Disclosures

- IV. Failure to maintain records including KYC details
- V. Unreasonable fees charged to clients
- VI. Failure to obtain requisite certification for employees of the company
- VII. Failure to Segregate Advisory and Execution Services
- VIII. Non-compliance with conditions of certificate of registration

DETAILED CHARGES AND APPRECIATION OF EVIDENCE

9. I shall now proceed to discuss the charges/allegations in detail, gist of the reply and my findings thereon.

I. Risk Profiling of clients and Suitability of Advice to Clients/Investors

(i) On the aspect of risk profiling, the Inspection report had recorded that the risk profiling questionnaire (hereinafter referred to as "**the questionnaire**") does not contain the basic information to be sought from the client which is necessary for the purpose of providing the investment advice such as the investment objective, client capacity for absorbing loss as specified in IA Regulations, etc.. Further the inspection report records that the risk assessment and risk profiling of the clients is not being done before selling the product to them and that many of the fields in the questionnaire were not filled up and CapitalVia is not obtaining such information from the clients, and the risk profile of the client is neither communicated to the client after risk assessment is done nor updated periodically.

In its Reply CapitalVia states *inter alia*- '*CapitalVia has an appropriate process for assessment of the risk of the clients by the experienced research team which undertakes the intensive exercise of assessment... by following scientific methodology with the help of computer aided software and technology. These risk profiles are frequently checked by feeding dummy data to ensure the accuracy of the results. It may also be noted that the independent compliance auditor also undertakes the risk profile exercise by feeding dummy data to ensure correctness of the results. The effectiveness of the research tools and analysis*

methods are verified from time to time to identify its limitations.' CapitalVia has sought to demonstrate how each of the questions stated in the questionnaire relates to the clauses of regulation 16 dealing with risk profiling of the client/investor. Further it states that it has modified the questionnaire pursuant to discussions with the inspection team of SEBI, and has now started to communicate the risk profile of the client pursuant to advice given by the SEBI officials.

(ii) On the aspect of suitability of advice provided to the clients, the Inspection report recorded *inter alia* that irrespective of whether a product is suitable or not, the same was being advised to the client, if the investor opts for that product. It was also observed that CapitalVia does not have a documented process for selecting investments based on client's investment objectives and financial situation and does not have a reasonable basis for investment recommendations vis-a-vis client's investment objectives, risk appetite or capacity for absorbing loss. In its Reply, CapitalVia *inter alia*, stated as follows: *'CapitalVia has developed in-house process for identification and selection of investment based upon intensive research by using scientifically developed tools and in-depth study of the securities. However all the securities are subject to the market risk but the endeavour of the CapitalVia is to minimize any such risk and keep the investors away from risky securities. The act of CapitalVia is merely as an advisor and the ultimate decision is taken by the investors. CapitalVia provides advise relating to intra day trading to all its clients and all the products are designed in such a way that they become suitable for intraday trading. The clientele of CapitalVia consists of persons who carried out intraday trading. The list of products that was offered to the clients was disclosed to SEBI at the time of registration through vide letter dated March 10, 2014. The recommendation / investment advice is based on technical analysis derived by studying historical charts, price, pattern and indicators to predict the future price movements by applying proper risk management technics.'*

CapitalVia has enclosed a format in which information is sought from clients for the purpose of rendering investment advice as one of the annexures to its Reply as well as the Written Submissions.

(iii) **Relevant Provisions of law:** Regulations 16 and 17 dealing with Risk Profiling and Suitability of Advice, respectively read as under-

"Risk profiling.

16. *Investment adviser shall ensure that,-*

- (a) *it obtains from the client, such information as is necessary for the purpose of giving investment advice, including the following:-*
- (i) *age;*
 - (ii) *investment objectives including time for which they wish to stay invested, the purposes of the investment ;*
 - (iii) *income details;*
 - (iv) *existing investments/ assets;*
 - (v) *risk appetite/ tolerance;*
 - (vi) *liability/ borrowing details.*
- (b) *it has a process for assessing the risk a client is willing and able to take, including:*
- (i) *assessing a client's capacity for absorbing loss;*
 - (ii) *identifying whether client is unwilling or unable to accept the risk of loss of capital;*
 - (iii) *appropriately interpreting client responses to questions and not attributing inappropriate weight to certain answers.*
- (c) *where tools are used for risk profiling, it should be ensured that the tools are fit for the purpose and any limitations are identified and mitigated;*
- (d) *any questions or description in any questionnaires used to establish the risk a client is willing and able to take are fair, clear and not misleading, and should ensure that:*
- (i) *questionnaire is not vague or use double negatives or in a complex language that the client may not understand;*
 - (ii) *questionnaire is not structured in a way that it contains leading questions.*
- (e) *risk profile of the client is communicated to the client after risk assessment is done;*
- (f) *information provided by clients and their risk assessment is updated periodically.*

Suitability.

17. *Investment adviser shall ensure that,-*

- (a) *All investments on which investment advice is provided is appropriate to the risk profile of the client;*
- (b) *It has a documented process for selecting investments based on client's investment objectives and financial situation;*
- (c) *It understands the nature and risks of products or assets selected for clients;*
- (d) *It has a reasonable basis for believing that a recommendation or transaction entered into:*
- (i) *meets the client's investment objectives;*

- (ii) *is such that the client is able to bear any related investment risks consistent with its investment objectives and risk tolerance;*
 - (iii) *is such that the client has the necessary experience and knowledge to understand the risks involved in the transaction.*
- (e) *Whenever a recommendation is given to a client to purchase of a particular complex financial product, such recommendation or advice is based upon a reasonable assessment that the structure and risk reward profile of financial product is consistent with clients experience, knowledge, investment objectives, risk appetite and capacity for absorbing loss.*

Further regulations 15(1) and 15 (9) read with clauses 2 and 4 of the Third Schedule (dealing with Code of Conduct for Investment Advisers) are also relevant in this regard. They read as under:

"General Responsibility.

15. (1) An investment adviser shall act in a fiduciary capacity towards its clients and shall disclose all conflicts of interests as and when they arise.

...

(9) An investment adviser shall abide by Code of Conduct as specified in Third Schedule.

Code of conduct

2. Diligence

An investment adviser shall act with due skill, care and diligence in the best interests of its clients and shall ensure that its advice is offered after thorough analysis and taking into account available alternatives.

4. Information about clients

An investment adviser shall seek from its clients, information about their financial situation, investment experience and investment objectives relevant to the services to be provided and maintain confidentiality of such information. "

(iv) **Finding:** It is revealed from the website of Capital Via that most of their products are oriented towards short term horizon of intraday to 3 months and not many products are simple enough for the investor to understand their inherent risks. Such short term horizon is more appropriate and suitable for only high risk investors and hence by selling such products for low/moderate risk investors, CapitalVia was diluting the norm of suitability. Therefore the generalised submissions of CapitalVia that they engaged with the customer at every stage to make him aware of the risk and to follow stop-loss and rules of disciplined trading do not hold merit.

Regulations 16 and 17 provide illustrative measures towards ensuring systematic risk profiling and suitability of advice rendered. Clauses 2 and 4 of the Third Schedule (Code of Conduct) to the IA Regulations reinforce the principle that investment advisers must provide advice only after collection of necessary information and detailed analysis while keeping the overall financial interest of investors in mind. The technological/ automated process adopted by CapitalVia for the purpose of risk assessment of a client obviating an interaction with the risk management team of the noticee is not sufficient to meet the level of assessment contemplated in the Regulations. Rather, the software systems and automations are a ruse to cover up the lack of application of mind to individual clients. The risk assessment must be both scientific and based on a proper appraisal/assessment of the investors ability to absorb risks and appreciate market processes. From the regulatory perspective, itemised mandate in the regulations is contemplated for strict adherence by registered investment advisers to ensure that the process of assessment of risk and suitability is meticulous. Any lapse in this regard, howsoever minor, is a serious infraction and cuts at the root of the premise on the basis of which the regulation of investment advisory activity has been anchored.

I have perused the submissions of CapitalVia and in particular the risk profiling questionnaire enclosed as an annexure to the reply and written submissions. As per the enclosure, the risk profile is calculated by providing different weighted values to investment of customer, age group and risk appetite, adding the same and dividing by three to arrive at the 'average score'. Even from a bare reading of the questionnaire and the 'formula' used to calculate the 'score' for a customer, it is amply clear that the entire process is very rudimentary without taking into account the asset and liability profile of the customer his income/expenditure pattern and his overall financial ability to bear losses. The format provides for the risk appetite to be measured only in terms of willingness and disregards his financial capacity. The questionnaire thus does not display

any scientific process of risk profiling. Obviously poor risk analysis leads to unsuitable investment advice resulting in loss to the investors.

After having given an opportunity of hearing to the Noticees and considering its submissions, I have also taken into account certain communications made by CapitalVia with SEBI after the Inspection Report had been communicated to them. The content of the letters dated July 17, 2015 and November 05, 2015 as well as email dated December 12, 2015, all from CapitalVia, reveal the following :

- a. While CapitalVia is claiming that the risk assessment and risk profiling of the clients is being done before selling the product to them with the help of in-house software 'GROOT', the GROOT software was developed by CapitalVia and came into effect from September 04, 2015 i.e. 18 months after the registration. CapitalVia has not submitted the information pertaining the process of risk profiling carried out by it before September 04, 2015.
- b. CapitalVia has started categorizing the products as High Risk, Medium risk and Moderately high risk from July 2015. CapitalVia has admitted that this system categorizing the clients is pursuant to the advice given by the inspection officials. There is no mention of what objective process was being followed for the purpose of risk assessment prior to July, 2015.

From the above, I am inclined to conclude that while the risk-profiling and risk assessment processes were completely absent before the middle of 2015, even the existing process employed by CapitalVia lacks any rational and scientific basis. These clearly tantamount to breach of regulations 16 and 17 along with Clauses 2 and 4 of the Third Schedule to the IA Regulations.

II. Non-compliance with fiduciary obligations and responsibilities and not acting with due skill, care and diligence

(i) The Interim Order recorded two instances of non-compliance with CapitalVia's fiduciary obligation towards its clients/investors:

- free trial services to the prospective clients without any thorough analysis of their needs and without acting with due skill, care and diligence
- not taking any fiduciary responsibility in respect of the advice provided to the clients and placing disclaimers effectively avoiding any responsibility in respect of its investment advice.

In its Reply, CapitalVia contended that it has a risk profiling process. However it has admitted that it has suitably amended the risk profiling and risk assessment process and started communicating the same to the client prior to the free trial. In the Written Submissions, CapitalVia states that they onboard any new customer only after Free Trial or once he has experienced the services in simulation so that he is educated enough to understand the risk and reward involved in the financial markets. Regarding the disclaimers, CapitalVia in its Reply has submitted that the motive of disclaimer is to provide him the real picture of the market without which it may give an assurance to the investor about returns that would be against the fundamental principles of the capital market. CapitalVia also submits in its Reply and Written Submissions that it conducts many investor education programmes and have qualified personnel in the organisation.

(ii) Relevant provisions of law: The fiduciary position of an investment adviser with his client and the mandate to act with due skill, care and diligence are discussed in several provisions in the IA Regulations. In particular, regulations 15(1)&(9), 16 and 17; and

clauses 2 and 4 of the Third Schedule to the IA Regulations may be seen, extracts of which have already been reproduced above.

(iii) Finding: Since the significance of the risk assessment process and the significant role that an investment adviser plays in relation to the investor have already been elaborated earlier in this order, it goes without saying that these responsibilities highlight the fiduciary relationship that an investment adviser has with his client. He is expected to function in the best interests of the client and not shrug off the responsibility for his advice. At the same time, it would be far fetched to expect that every advice has to be accurate and financially rewarding for the client. Placing blanket disclaimers for every client's attention does not meet the standards laid down in the IA Regulations in terms of its service / relationship as an Investment Adviser.

Given that CapitalVia has admitted to certain infractions with respect to the free trial period, I do not consider it necessary to deliberate on the same further in this order, in the interest of brevity. The additional statements in the written reply regarding investor education programmes being conducted by them and the employment of qualified research analysts, though appreciable, do not directly address the concerns raised by SEBI. Further, the corrective measures are not backed by any tangible evidence. I therefore find CapitalVia to have violated provisions of regulations 15(1)&(9), 16 and 17; and clauses 2 and 4 of the Third Schedule to the IA Regulations.

III. False and Inadequate Disclosures

(i) Based on a perusal of the website, the Interim order recorded the prima facie conclusion that 'CapitalVia is not disclosing all required material information while soliciting and on boarding clients' and that the 'information disclosed by CapitalVia *prima*

facie appears to be inadequate for a prospective client to take a well informed decision.'

In its Reply, CapitalVia had submitted that they were in compliance with the mandate to make all material disclosures.

(ii) There are three specific aspects of false or misleading disclosures made by CapitalVia recorded in the Inspection report and confirmed by the Interim order which are relevant for consideration -

The Inspection Report had recorded that certain information disclosed on the website of CapitalVia i.e. www.capitalvia.com was incorrect/false. Specifically the information pertaining to advisory team, number of clients and offices in Singapore & USA, were found to be incorrect. Regarding the reference to advisory team, CapitalVia in its written reply stated that the intent of the reference to 'advisory team' "*indicates that a group of employees/ members in a team which may consist of various verticals of operations, includes research team, sales team, support staff team etc.*" Upon enquiry by the inspection team the number of employees specified on its website was revised downwards, and it was clarified that it only has virtual offices in USA & Singapore, with no employees physically working from those locations.

(iii) The Inspection report records *inter alia* that the performance track record communicated to the clients appears to be erroneous. In the method of calculation of performance track record, CapitalVia was taking into the consideration of only the profitable calls and not the loss making calls. Ideally it should have taken into consideration all the calls irrespective of the profit or loss. Further, it was noted that, though CapitalVia is calculating performance track record on a monthly basis, the accuracy rate disclosed on the website and in many of their e-mails sent to the clients is

static and is not being updated on a monthly basis. It prima facie appears that CapitalVia has not made any disclosure in respect of all material information about itself including its business, disciplinary history, the terms and conditions on which it offers advisory services, key features of the products or securities including performance track record, the warnings, disclaimers in documents, advertising materials relating to an investment product which it is recommending to the client, etc. as specified in IA Regulations.

In its reply, Capital Via has inter alia stated as follows- *'CapitalVia has made adequate disclosures of all material information about itself including its business history, terms and conditions. There is specific disclosure about advisory service fees payable by the client and the refund policy. It is also submitted that there is specific mention about the risk involved in dealing with securities and CapitalVia do not undertake any guarantee and responsibility for any loss suffered by the client. CapitalVia maintains all the records of the basis for arriving at investment advice which is undertaken by the qualified research analyst using the appropriate research analysis tools. The website of CapitalVia i.e. www.capitalvia.com contains all the relevant information as specified by the Regulation 18 of LA Regulations which includes its business, terms and condition on which CapitalVia offers advisory services, key feature of product etc.'*

(iv) The Interim Order took note of several websites which admittedly were used by CapitalVia for marketing purposes, and made the following adverse observations regarding failure to disclose relevant material information in the websites:

- The websites do not contain any reference to CapitalVia.
- There is no information with regard to whom the website belongs to and what are their contact details.
- There is no mention on the website about registration of CapitalVia as an investment adviser.

In its Reply and Written Submissions, CapitalVia stated that during the course of registration, SEBI officials had never objected to the act of CapitalVia soliciting clients through various websites. They also stated that such practices are common tools of advertising. Further they submitted that pursuant to the inspection, CapitalVia has stopped such acts with immediate effect.

(v) **Relevant Provisions of law** : Regulation 18 of the IA Regulations dealing with the obligation of making disclosures to clients reads as follows:

"Disclosures to clients.

18. (1) *An investment adviser shall disclose to a prospective client, all material information about itself including its business, disciplinary history, the terms and conditions on which it offers advisory services, affiliations with other intermediaries and such other information as is necessary to take an informed decision on whether or not to avail its services.*

(2) *An investment adviser shall disclose to its client, any consideration by way of remuneration or compensation or in any other form whatsoever, received or receivable by it or any of its associates or subsidiaries for any distribution or execution services in respect of the products or securities for which the investment advice is provided to the client.*

(3) *An investment adviser shall, before recommending the services of a stock broker or other intermediary to a client, disclose any consideration by way of remuneration or compensation or in any other form whatsoever, if any, received or receivable by the investment adviser, if the client desires to avail the services of such intermediary.*

(4) *An investment adviser shall disclose to the client its holding or position, if any, in the financial products or securities which are subject matter of advice.*

(5) *An investment adviser shall disclose to the client any actual or potential conflicts of interest arising from any connection to or association with any issuer of products/ securities, including any material information or facts that might compromise its objectivity or independence in the carrying on of investment advisory services.*

(6) *An investment adviser shall, while making an investment advice, make adequate disclosure to the client of all material facts relating to the key features of the products or securities, particularly, performance track record.*

(7) *An investment adviser shall draw the client's attention to the warnings, disclaimers in documents, advertising materials relating to an investment product which it is recommending to the client."*

Further clauses 1 and 5 of the Third Schedule to the IA Regulations also mandate adequate disclosures as well as honesty and fairness in its actions. The said clauses read as under:

"1. Honesty and fairness

An investment adviser shall act honestly, fairly and in the best interests of its clients and in the integrity of the market.

5. Information to its clients

An investment adviser shall make adequate disclosures of relevant material information while dealing with its clients."

(vi) **Finding:** As regards the conduct of the entity relating to disclosures, at the outset, it needs to be mentioned that CapitalVia is in breach of the directions contained in the Interim order and have continued to solicit new business by not de-activating the relevant functionalities in their website. Nor have they displayed the SEBI's order in their website, which would have dissuaded fresh advisory business. The response put forth by CapitalVia during the Hearing was hardly convincing as they took the stand that while the new client payment functionality is not de-activated, they refund whatever amount is paid by the new clients and telephonically informed them about the reason for refund. Display of the restraints imposed by SEBI's interim order on their website together with the de-activation of payment window for the new clients would have ensured compliance with the spirit of the Interim order but the non-compliance on this aspect clearly evidences a clear attempt to circumvent the SEBI order. This issue is more relevant when there is a charge of non-disclosures against CapitalVia in the Inspection report as well as the Interim order in the light of the mandate under the IA Regulations which casts an obligation on the IA to disclose all material information about itself to its clients. This is directly in violation of Regulation 18(1) which requires inter alia publication of disciplinary actions.

It appears from the Inspection report and the Interim order that the concerns with respect to disclosures primarily emanate from non-comprehensive information provided to clients, the lack of prompt updation of information, and erroneous/misleading information on performance track record. The documents enclosed as annexure to the Reply and Written submissions are merely statement of Terms and Conditions and Disclaimer. These documents do not really address the concerns pertaining to disclosures

by CapitalVia. The allegation that false disclosures relating to clients and offices in USA and Singapore have not been effectively rebutted with any satisfactory evidence. These false disclosures on the website of CapitalVia are a grave concern. Regarding soliciting of clients through various websites, I note that the charge against CapitalVia is not for using multiple websites to market themselves, but for lack of material information being disclosed in all such websites. Therefore the contention that SEBI, at the time of registration, had not objected to CapitalVia using multiple websites for marketing, is untenable. The regulatory framework of the securities market is a disclosure based one. Any attempt by an investment adviser to either conceal material information or to communicate information which is misleading and solely with the objective of increasing revenue, must be dealt with sternly. Infact this rule applies to all registered intermediaries and listed entities, and is viewed more stringently with those who have a direct interface with investors in the securities market. In view of the above, I find that CapitalVia has violated provisions of regulation 18 and clauses 1 and 5 of the Third Schedule to the IA regulations.

IV. Failure to maintain records including KYC details

(i) The Interim order noted that CapitalVia admittedly did not maintain records of KYC, risk profiling, risk assessment of the client and rationale of investment advice to its clients. These observations were made after taking into account the Inspection Report and the reply of CapitalVia to the Inspection Report. However in its Reply to the Interim Order and in its Written Submissions, CapitalVia has done a volte-face by stating it is maintaining all records including those pertaining to KYC of clients. CapitalVia has stated that all of its records, whether agreements, risk assessment, advice to clients, SMS

to clients etc are all maintained in digital form and are available with CapitalVia. It also stated in its Reply and Written Submissions that all voice calls are monitored by a dedicated internal department, and logs of the same are maintained.

(ii) **Relevant Provisions of law:** There are two provisions of the IA Regulations which are particularly relevant in this regard- one dealing with necessity to adhere to KYC procedure and the other dealing with the mandate to maintain all relevant records.

Regulation 15(8) in the context of KYC procedure reads as follows:

"(8) An investment advisor shall follow Know Your Client procedure as specified by the Board from time to time."

An earlier set of circulars applicable to all registered intermediaries mandated KYC obligations as follows:

- SEBI Circular No. MIRSD/SE/Cir-21/2011 dated October 05, 2011, stated *inter alia*- "the KYC form, specified as Annexure-I of the said circular, shall be filled by an investor at the account opening stage while dealing with SEBI registered intermediaries."
- SEBI circular no. MIRSD/Cir- 26 /2011 dated December 23, 2011, stated *inter alia* "after doing the initial KYC of the new clients, the intermediary shall forthwith upload the KYC information on the system of the KRA and send the KYC documents i.e. KYC application form and supporting documents of the clients to the KRA within 10 working days from the date of execution of documents by the client and maintain the proof of dispatch."

The aforesaid circulars were commonly applicable to all registered intermediaries. Therefore from the date that CapitalVia was registered as an investment adviser, the provisions of the said circulars would be applicable to it as well.

Regulation 19(1) of IA Regulations in the context of maintenance of records reads as follows-

"Maintenance of records.

19. (1) *An investment adviser shall maintain the following records,-*

- (a) Know Your Client records of the client;*
- (b) Risk profiling and risk assessment of the client;*
- (c) Suitability assessment of the advice being provided;*
- (d) Copies of agreements with clients, if any;*
- (e) Investment advice provided, whether written or oral;*
- (f) Rationale for arriving at investment advice, duly signed and dated;*
- (g) A register or record containing list of the clients, the date of advice, nature of the advice, the products/ securities in which advice was rendered and fee, if any charged for such advice.*

(2) All records shall be maintained either in physical or electronic form and preserved for a minimum period of five years:

Provided that where records are required to be duly signed and are maintained in electronic form, such records shall be digitally signed.

(3) An investment adviser shall conduct yearly audit in respect of compliance with these regulations from a member of Institute of Chartered Accountants of India or Institute of Company Secretaries of India."

(iii) **Finding:** As noted above, CapitalVia has not been consistent in its replies. This is seen from their responses to the inspection report and the Replies sent subsequently. As I have already elaborated at the outset, the Internal Audit Report is not sufficiently credible to be relied upon for the purpose of arriving at a conclusion on the status of compliance by CapitalVia. The reliance therefore by CapitalVia on the said Audit Report to back its claims of compliance cannot be accepted. A mere rebuttal of allegations without providing necessary evidence to back their claims may not help the case of CapitalVia. Maintenance of stipulated records is a discipline required from all registered intermediaries and is all the more an ethical responsibility of intermediaries who are in direct relationship with investors. Most importantly, compliance with SEBI (KYC Registration Agency) Regulations, 2011, was stipulated as a condition by SEBI at the time of grant of registration, communicated vide letter dated May 19, 2014. Considering

available documents and statements, I find that CapitalVia has violated provisions of regulation 15(8) and regulation 19 of the IA Regulations, and Circulars dated October 05, 2011 and December 23, 2011 issued by SEBI under section 11(1) of the SEBI Act, 1992, as pointed out in the inspection report

V. Unreasonable fees charged to Clients

(i) The Interim order took note of the Inspection report findings that CapitalVia had charged huge fees from clients without any justification. It also took note of one of the complaints wherein the complainant was charged an advisory fee of ` 24,59, 856/- even though as per the complaint, the intended amount of investments was only between 6 and 10 lakh rupees. The interim order taking note of all the available information concluded that CapitalVia has charged unreasonable fee from its clients. In its Reply as well as Written Submissions, CapitalVia has stated that they incur substantial expenditure on skilled manpower and high end technology. In the Written Submissions, CapitalVia has stated that the fee charged is based on various factors namely, 'experience of the analyst serving, frequency of involvement, tenure of subscription, number of products subscribed to, standard of service & support expectations of a customer and the cost-efforts of operations while serving this exclusive customer.' As an annexure, the Written Submissions also enclose a Fee Matrix. Further, CapitalVia has stated that there is no regulatory guidelines on fees and charges by Investment Adviser. In the Written Submissions, CapitalVia has also submitted that less than 5% of customers are charged more than Rs 1.5 lakh and therefore the allegation of CapitalVia charging exorbitant fees does not hold true.

(ii) **Relevant provisions of law:** Clause 6 of the Code of Conduct for investment advisers, stipulated in the Third Schedule to the IA Regulations states as follows-

"Fair and reasonable charges.

*An investment adviser advising a client may charge fees, subject to any ceiling as may be specified by the Board, if any. The investment adviser shall ensure that fees charged to the clients is **fair and reasonable.** "*

(emphasis supplied)

(iii) **Finding:** The exorbitant fee to the extent of four times the amount of investment involved for which the Investment Advice is rendered indicates that CapitalVia is doing more than mere advisory services for its clients though the receipts are shown towards fees collected. It was not possible for me to seek the complainants' version about the payment owing to the timelines set in the matter. However, the stand that the combination of skilled manpower and high ended technology comes at a high cost for HNIs is not satisfactory and leaves room for suspicion.

Further, an extension of the principle for investment advisers to act with due care and observing its fiduciary relationship with clients, is the mandate not to charge unreasonable fees from clients. SEBI has not specified any guidelines for charging fees since this is a commercial aspect into which a regulator need not intervene. However a broad guideline to ensure reasonableness in charging fees has been provided in the Code of Conduct as noted above. There is a strong rationale for the regulations indicating the reasonableness of charges. Apart from the fact that reasonable charges ensure that even small and medium sized investors have access to financial markets, unjustifiably high charges play a significant role in fuelling unrealistic expectations on the part of investors. This in turn forces the investors to opt for highly risky products, completely unsuitable to his profile, pushing his investments into a highly vulnerable zone.

I have perused the 'Fee Matrix' submitted by CapitalVia as part of its Written Submissions. However this so-called fee matrix does not help to determine the reasonableness of the fees charged. Ofcourse it does indicate more services for a higher

quantum of fee. But this per se appears insufficient to conclude that the fee charged is commensurate with the services provided. It is important for CapitalVia to demonstrate to its clients that the fees levied by them is fair and reasonable as against the advice rendered in terms of reliability, duration of the advice, accuracy and suitability and not in terms of the expected returns to the client. Since there are investor complaints in relation to high fees charged, it indicates the lack of investor confidence in the rationale for such high charges. While it is difficult to conclude that CapitalVia committed a breach of clause 6 of the Third Schedule to the IA Regulations on the above basis, I am of the opinion that CapitalVia needs to be far more responsible in calibrating its fee structure, which is consistent across products and clients, keeping in mind the amount under the scope of investment advice.

VI. Failure to obtain requisite certification for employees of the company

(i) The Interim Order records that all representatives of CapitalVia have not complied with the certification requirements specified in the IA Regulations. This conclusion was arrived at based on the Inspection Report findings that out of the total number of approximately 60 employees who are representatives, only 19 have obtained both Level I and Level II certifications for investment advisers.

In its Reply, CapitalVia has submitted that at present there are approximately 38 research analysts working with them. It is gathered that these 38 research analysts qualify to be representatives of CapitalVia in terms of regulation 2(1)(r) of the IA Regulations. They have further submitted that all these 38 research analysts have the requisite certification. To prove their submissions they have annexed copies of NISM certificates of all the research analysts employed with CapitalVia.

(ii) **Relevant provisions of law:** Regulation 7(2) of the IA Regulations reads as under:

*"(2) An individual registered as an investment adviser and partners and **representatives** of investment advisers registered under these regulations offering investment advice shall have, at all times, a certification on financial planning or fund or asset or portfolio management or investment advisory services:*

(a) from NISM; or

(b) from any other organization or institution including Financial Planning Standards Board India or any recognized stock exchange in India provided that such certification is accredited by NISM.:

Provided that the existing investment advisers seeking registration under these regulations shall ensure that their partners and representatives obtain such certification within two years from the date of commencement of these regulations:

Provided further that fresh certification must be obtained before expiry of the validity of the existing certification to ensure continuity in compliance with certification requirements. "

(emphasis supplied)

The word 'representative' has been defined in regulation 2 (1)(r) of the IA Regulations to mean *"an employee or an agent of an investment adviser **who renders investment advice on behalf of that investment adviser"**.*

(iii) **Finding:** I have perused the NISM certificates enclosed by CapitalVia as Annexure R-12 along with its reply, and I find that out of the 38 Research Analysts/Representatives employed by CapitalVia, five(5) have not completed both levels of NISM certification. Further, the SEBI notification requiring NISM certification had prescribed April 20, 2015 as being the deadline for obtaining both Level-1 and Level-2 certifications. I note from the certificates submitted that 15 persons did not obtain Level-1 certification within the said deadline, and 31 persons failed to obtain Level-2 certification within the said deadline. This establishes the breach of Regulation 7(2) by CapitalVia.

VII. Failure to segregate Advisory and Execution Services

(i) The Interim order recorded that CapitalVia admittedly has provided advisory services coupled with execution services without any segregation and maintaining an

arms-length relationship between investment advisory activity and execution activity. The said finding was based on the Inspection Report observation that, few employees of CapitalVia are involved in providing advisory and execution services at the same time, and upon enquiry CapitalVia has submitted that, it has obtained authorization from the clients to trade on their behalf. In its Reply, CapitalVia inter alia stated the following: *"...the recommendation were served only to the persons whose number were referred by the client and was registered with us. ...It is important to put once again on record that CapitalVia is not associated with any other entity involved in execution services..."* In the Written Submissions, CapitalVia reiterated that they have no financial interest or relationship with any execution service provider of any of their customers. During the Hearing the representative of CapitalVia admitted that on certain occasions, as requested by the clients, stock tips or investment advice were sent as mobile phone alerts which may be forwarded to the brokers/agents assigned by the clients/investors. But no financial benefits accrued from such relationship, and such forwarding of investment advice is only to facilitate the clients/investors and not by way of execution services.

(ii) **Relevant Provisions of Law:** Regulation 22 of the IA Regulations reads as follows:

"Segregation of execution services.

1. 22. *Investment advisers which are banks, NBFCs and body corporate providing distribution or execution services to their clients shall keep their investment advisory services segregated from such activities:*

2. *Provided that such distribution or execution services can only be offered subject to the following:*

- (a) The client shall not be under any obligation to avail the distribution or execution services offered by the investment adviser.*
- (b) The investment adviser shall maintain arms length relationship between its activities as investment adviser and distribution or execution services.*
- (c) All fees and charges paid to distribution or execution service providers by the client shall be paid directly to the service providers and not through the investment adviser. "*

(iii) **Finding:** The inspection report recorded that during the inspection it was observed that, few employees of CapitalVia are involved in providing advisory and execution services at the same time, and upon enquiry CapitalVia has submitted that, it has obtained authorization from the clients to trade on their behalf. I note that the Interim Order itself records that as per details submitted, CapitalVia had obtained authorization from 10 clients.

The provisions of regulation 22 clearly mandate that a body corporate having advisory services as well as execution/distribution business, must ensure a segregation between such businesses. CapitalVia denies that it provides any execution services but has admitted to have forwarded investment advice as authorized/requested by the clients/investors. In such cases, it may not be absolutely clear whether the allegation of non-compliance with regulation 22 will apply since it appears that CapitalVia is otherwise not in the course of rendering execution services. Further while there may be an infraction, the instances of authorization taken from clients do not appear to be significant enough to warrant any adverse finding. Nonetheless, CapitalVia is directed to ensure that its actions be in strict compliance with the letter and spirit of regulation 22 of the IA Regulations.

VIII. Non-compliance with conditions of certificate of registration

(i) The Interim order found that CapitalVia was in breach of the statutory obligation to use the words 'investment adviser' in its name. In its Reply, CapitalVia submitted that corrective action had been taken and required changes have been made.

(ii) **Relevant Provisions of law:** Regulation 13(c) of the IA Regulations reads as follows:

(c) the investment adviser, not being an individual, shall include the words 'investment adviser' in its name:

Provided that if the investment advisory service is being provided by a separately identifiable department or division or a subsidiary, then such separately identifiable department or division or subsidiary shall include the words 'investment adviser' in its name;

(iii)**Finding:** CapitalVia has admitted to it having violated the mandate to use the words 'investment adviser' in its name, and assured that corrective measures have been taken. However I note that in correspondences even subsequent to the Inspection Report, I do not find reference to the words 'Investment Adviser'. If CapitalVia is sincere about its assurance, it must take tangible measures to ensure that its status of being an Investment Adviser is sufficiently and clearly displayed in all communications with members of the public as well as with its clients. This regulatory mandate forms part of the principle of disclosing material information. Though the assurance for rectification is welcome, CapitalVia was clearly in breach of the provisions of regulations 13(c) of the IA Regulations.

10. Registration of investment advisers is a statutory mandate flowing from section 12 (1) of the SEBI Act, 1992. Regulation of Investment advisory activity was considered necessary to avoid unscrupulous advisory business wherein investors could be misguided towards making investments in the securities market. There was a need to ensure discipline in this field of intermediation business in the securities market. Quality of advice rendered to investors has an impact on investors confidence in the integrity of the markets. Consequently, it is statutorily and ethically important to view seriously any infraction on the part of investment advisers. This is all the more so in the case of a large organization like CapitalVia which by its own statement is considered to be a pioneer in the field of investment advisory business. The more significant an organization, the bigger the ripple effect its actions or omissions have on the confidence in the system. Broadly, the submissions made by CapitalVia are in the nature of admissions to the alleged violations, along with statements that they have taken rectification measures. In other

instances, as already noted in the discussion above, no effort has been made to disprove the allegations against them, except for statements of rebuttal. Bland statements without necessary proof will not lend credence to the defence of CapitalVia. Further, the submissions on the part of CapitalVia have neither been consistent, nor are backed by sufficient proof.

11. To sum up, amongst the violations, the most serious violation is of non-disclosure to the clients including non-dissemination of restraint orders of SEBI, followed by the improper risk evaluation and dissemination processes. Though I take on record, the rectification measures adopted by CapitalVia with respect to maintenance of records, KYC details, obtaining certifications and compliance with the conditions of registration, CapitalVia needs to exercise a better sense of responsibility towards its clients and adhere to the mandates of the IA Regulations by strict compliance. Considering the gravity of the material suppressions that had been done by CapitalVia and its lack of diligence to ensure adherence to the prescriptions of law, I find it necessary to pass suitable directions. In view of the above findings and observations, in the interest of securities market and with the objective of protecting the interest of investors, I, in exercise of the powers conferred upon me under sections 11(1), 11B and 11D of the Securities and Exchange Board of India Act, 1992, hereby direct as follows:

- (i) That the directions not to solicit or undertake any fresh advisory business shall continue against CapitalVia and its above named Directors for another period of four months from today.
- (ii) That CapitalVia shall discontinue the acceptance of funds from clients including by way of deactivation of online remittances, with immediate effect during the aforesaid four month period.
- (iii) That CapitalVia shall disclose the contents of these directions prominently on its website(s) immediately

12. The verification of adherence to the provisions of IA Regulations and the directions contained in this Order may be separately carried out by SEBI and in case of detection of any non-compliance, suitable action under law shall follow.

Place: Mumbai

Date: January 20, 2017

G. MAHALINGAM
WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA