NATIONAL COMMODITY & DERIVATIVES EXCHANGE LIMITED

Circular to all members of the Exchange
Circular No. : NCDEX/COMPLIANCE-152/2023
Date : December 26, 2023
Subject : Order in the matter of M/s Steel City Commodities Pvt. Ltd.

Members and their constituents are hereby informed that the Securities and Exchange Board of India has vide its order no. WTM/AS/MIRSD/DOP/29895/2023-24 dated December 22, 2023 against M/s. Steel City Commodities Pvt. Ltd. inter alia directed as under:

"…prohibit the Noticee i.e. Steel City Commodities Private Limited bearing Certificate of Registration (bearing No. INZ000076330) from trading in proprietary capacity and taking up any new clients for a period of fifteen (15) days from the date of this Order or till the FIR filed against the Noticee by EOW ceases to be pending or the Noticee is discharged or acquitted by a Court in relation to the FIR, whichever is later…."

A copy of the said order is enclosed for your reference.

In view of the above, Members and their constituents are advised to take note of the same and ensure compliance.

For and on behalf of
National Commodity & Derivatives Exchange Limited

Smita Chaudhary
Senior Vice President - Compliance

For further information / clarifications, please contact

1. Customer Service Group on toll free number: 1800 26 62339
2. Customer Service Group by e-mail to: askus@ncdex.com

WTM/AS/MIRSD/DOP/29895/2023-24

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.
STEEL CITY COMMODITIES PRIVATE LIMITED	**INZ000076330**

In the matter of National Spot Exchange Limited

BACKGROUND

1. The present proceedings originate from the Enquiry Report dated February 28, 2020 (hereinafter referred to as the **"Enquiry Report)**, submitted by the Designated Authority (hereinafter referred to as the **"DA"**) in terms of Regulation 27 of the Securities and Exchange Board of India (Intermediaries) Regulations, 2008 as it stood at the relevant point of time prior to its amendment vide Securities and Exchange Board of India (Intermediaries) (Amendment) Regulations, 2021, with effect from January 21, 2021, (hereinafter referred to as the **"Intermediaries Regulations"**), wherein the DA, based on various factual findings and observations so recorded in the said Enquiry Report, recommended cancellation of the certificate of registration granted to Steel City Commodities Private Limited (hereinafter referred to as the **"Noticee"**). Pursuant to the same, a Post Enquiry Show Cause Notice dated March 18, 2020 (hereinafter referred to as the **"SCN"**) was issued to the Noticee, along with the copy of the aforesaid Enquiry Report, copy of letter dated December 30, 2014 of Department of Economic Affairs, Ministry of Finance and copy of the decision of the Hon'ble Bombay High Court dated August 22, 2014 in respect of paired contracts offered on the platform provided by the National Spot Exchange Limited (hereinafter referred to as the **"NSEL")**.

2. While the aforesaid proceedings were pending, Securities and Exchange Board of India (hereinafter referred to as the **"SEBI"**) passed five separate orders during February 2019, rejecting the applications filed by five other entities for registration as commodity brokers who were involved in NSEL matter. Aggrieved by the said SEBI orders, the entities filed separate appeals before the Hon'ble Securities Appellate Tribunal (hereinafter referred to as the **"Hon'ble SAT"**). The Hon'ble SAT, vide its common order dated June 09, 2022 (hereinafter referred to as **"SAT order"**), remanded the aforesaid SEBI orders to SEBI to decide these matters afresh within six months from the date of the said order. While remanding the aforesaid SEBI orders, the Hon'ble SAT, *inter alia*, held as under:

> *"42…The matters are remitted to the WTM to decide the matter afresh in the light of the observations made aforesaid in accordance with law after giving an opportunity of hearing to the brokers. All issues raised by the brokers for which a finality has not been reached remains open for them to be raised before the WTM. It will be open to the WTM to rely upon other material such as the complaint letters of NSEL, EOW report, EOW charge sheet, etc. provided such copies are provided to the brokers and opportunity is given to rebut the allegations. Such additional documents relied upon by the respondent should form part of the show cause Notice for which purpose, it will be open to the WTM to issue a supplementary show cause Notice…"*

3. Thereafter, the Competent Authority of SEBI allocated the present matter to me for further proceedings. In light of the aforesaid SAT order, it was felt necessary to furnish certain additional documents/ material to the Noticee and grant an opportunity of personal hearing, before concluding the present proceedings. Accordingly, vide Hearing Notice dated November 10, 2022 (hereinafter referred to as the **"Hearing Notice"**), Noticee was provided an opportunity of personal hearing on December 13, 2022 along with certain additional documents/ material. Noticee was also advised to submit its response, if any, in relation to the Hearing Notice. The hearing was adjourned on multiple occasions and was finally concluded on July 21, 2023. On the scheduled date of hearing, the authorised representatives of the Noticee appeared on behalf of the Noticee and made submissions on the lines of the replies submitted earlier.

4. The submissions filed by the Noticee vide its letters dated July 29, 2020, September 08, 2020, December 09, 2022, February 20, 2023, July 15, 2023, July 24, 2023 and August 14, 2023 are summarized hereunder:

(i) There is an inordinate delay in initiation of the proceedings.

(ii) The Noticee has not been provided with all the relevant, vital and material information and documents while issuing the SCN.

(iii) An opportunity of hearing has not been provided by the DA before issuance of SCN.

(iv) The alleged transactions were executed on January 28, 2013 and March 08, 2013 on behalf of only one of its clients out of 7500 registered across all the stock exchange i.e. Mr. Peddi Govinda Rao and that too for two days. All the post trade Pay in and payout of funds and commodities were carried out by clearing and settlement department of NSEL in a timely manner.

(v) On behalf of the client, the Noticee has paid Value Added Tax and warehousing charges as applicable and the same has been recovered from the client on March 26, 2013

(vi) The Noticee has also provided an affidavit dated June 19, 2020 from the client, Mr. Peddi Govinda Rao which *inter alia* states that he had executed the trades on the basis of information available on NSEL website and no advice or inducement was given to him by the broker.

(vii) The trade carried out by client fulfills all the conditions laid down in exemption notification dated June 05, 2007.

(viii) NSEL had been openly carrying out trading in a variety of commodities and the details of the same were being regularly reported to the Forward Market Commission (“FMC”).

(ix) Since FMC was performing the function of a regulator over NSEL from August 2011, the Noticee had no reason to doubt the legality or validity of these contracts.

(x) There was gross failure of FMC in performing its duties as an apex regulator of commodities market and its presence as a mere silent spectator is the root cause of the subject matter of the present proceedings.

(xi) No adverse remarks/red flags were raised against various agencies like MMTC, FCI, NAFED, etc. that had executed trades on the NSEL platform as clients and who were also purported to be closely associated with NSEL. Hence the dealings of the Noticee on the NSEL trading platform should also be considered along the similar lines.

(xii) The first leg of the alleged paired contract was always a "purchase" and the Noticee had fulfilled its trading obligations on execution of buy and sell contracts independently and had made full payment of consideration of the buy contract.

(xiii) Except having a member/ broker relationship with NSEL, the Noticee had no other connection or association with NSEL, its directors, promoters and key management persons in any manner whatsoever. Except earning the meagre brokerage on execution of trades on 2 days on behalf of only one client, the Noticee had not derived any gain or benefit of any nature whatsoever.

(xiv) While granting registration to it, SEBI was fully aware that the Noticee had carried out the trades in the alleged paired contracts and therefore the principles of *res judicata* and *estoppel* would apply.

(xv) At the relevant time, SEBI was not the regulator of the NSEL and therefore, SEBI is not empowered to initiate any action against the Noticee under the provisions of the Intermediaries Regulations. SEBI ought not to initiate any action under Regulation 23 of the Intermediaries Regulations as there was no violation of any securities market law at relevant time.

(xvi) It was NSEL which introduced the concept of alleged 'paired contracts' and the Noticee as broker had no role in NSEL deciding to launch such paired contracts. No court or authority had ever held or even alleged that any contracts were launched by the NSEL without the prior concurrence of FMC as stipulated in NSEL Bye-Laws.

(xvii) In view of the order of the SAT dated June 09, 2022, the various orders judgments/ reports passed/ issued by various regulatory authorities as referred in the Enquiry Report cannot be considered and observations in respect of the same should be quashed and set aside.

(xviii) The Hon'ble Supreme Court in its Order dated April 30, 2019 in the matter of *63 Moons Technologies* has not made any adverse observations or finding against it or any other non-defaulting broker.

(xix) No flaws, non-compliances, deficiencies and breaches of trading in commodities were pointed out by any government department, FMC or by any other regulatory authorities.

(xx) The amendment to the fit and proper criteria of the Intermediaries Regulations is not applicable to the Noticee since the said amendment with respect to consideration of the 'criminal complaint' was with effect from November 17, 2021. However, the FIR against the Noticee was filed way back in 2018.

(xxi) Such retrospective application of the amendments to the Intermediaries Regulations, which are substantive provisions, is in gross violation of the principle of natural justice.

(xxii) FIR is only the first instance of reporting of a complaint that is lodged with the Police which is a preliminary document based on the one sided statement of the complainant without any adjudication of the same. Thus, SEBI cannot rely on its own complaint dated September 24, 2018 pursuant to which FIR dated September 28, 2018 was filed.

(xxiii) The Observations of SAT in the matter of *Almondz Global Securities Ltd. vs SEBI* and Order dated October 18, 2022 passed by the Hon'ble Bombay High Court in the matter of *Geeta Lunch Home Vs State of Maharashtra & Ors*. were referred to contend that merely the filling of an FIR and no proven charge against it, should not be a ground to cancel its license.

(xxiv) It is illogical to contend that anyone who dealt in the alleged paired contracts as a member of NSEL would be declared as not a fit and proper person.

(xxv) The important criteria of being fit and proper i.e., 'reputation', 'integrity', 'character', 'fairness' and 'competence' was consistently fulfilled by the Noticee.

(xxvi) The trading in NSEL was open and transparent and there was nothing surreptitious about it and no authority had ever questioned the legitimacy or validity of any contract/ trade;

(xxvii) The entire ecosystem of NSEL was similar to all other Exchanges and there were no 'red flags' to arouse any suspicion;

(xxviii) Till the time the Noticee continued to act as a broker of NSEL, the reputation of NSEL had not been tarnished;

(xxix) The Noticee was not on any committee or the Advisory Board of NSEL and there was no relationship between NSEL and the Noticee apart from the member and exchange;

(xxx) MCX and NSEL had common directors and common shareholding and thus the two were closely associated but no proceedings have been initiated against MCX. On the other hand, the Noticee had no actual 'association' with the NSEL;

(xxxi) The doctrine of proportionality and Wednesbury Rule/ Test should be consistently applied to ensure that relevant vital and material facts have been taken into consideration. It is a settled law that the punishment should not only be reasonable but must fit the violation or breach of law for which the entity is sought to be penalised. The same is squarely applicable in the present case.

(xxxii) Vide letter dated November 20, 2015, Ministry of Finance directed SEBI not to exercise any 'regulatory function' in respect of NSEL.

(xxxiii) In terms of regulation 5(e) of the Stock Brokers Regulations, the 'fit and proper person' criteria is looked into at the time of granting of certificate of registration and the Noticee was duly compliant with the criteria at the time of grant of certificate of registration.

(xxxiv) Noticee has executed the contracts with utmost integrity and adhered to soundness, moral principles and character in terms of Clause A(1) of the Code of Conduct under the Stock Brokers Regulations.

(xxxv) Clause A(2) of the Code of Conduct of Stock Brokers Regulations mandates a stock broker to act with due skill, care and diligence and the Noticee has duly exercised such due skill, care and diligence as a man of ordinary prudence is expected to do. The alleged violation of Clause A(5) of the Code of Conduct under the Stock Brokers Regulations is denied.

(xxxvi) Noticee has complied with the Rules, Regulations of SEBI and bye laws of the exchange(s).

(xxxvii) It is submitted that in view of the additional documents and circumstances the matter ought to be remitted to the DA in terms of Regulation 27(3) of the Intermediaries Regulations.

(xxxviii) Noticee's name is not mentioned in the chargesheet filed by EOW in the matter.

(xxxix) The Noticee is also registered with Insurance Regulatory and Development Authority and its membership is renewed on March 31, 2022. Thus, it is submitted that the Noticee is a Rule Compliant entity.

CONSIDERATION OF ISSUE AND FINDINGS

5. I have carefully perused the SCN, the Hearing Notice, the Enquiry Report, the replies filed by the Noticee and other material/ information available on record. After considering the allegations made/ charges levelled against the Noticee in the instant matter as spelt out in the SCN and Hearing Notice, the limited issue which arises for my consideration in the present proceedings is whether the Noticee satisfies the 'fit and proper' person criteria as laid down under Schedule II of the Intermediaries Regulations and whether the Certificate of Registration granted to the Noticee should be cancelled, as recommended by the DA or any other action should be taken against the Noticee.

6. Before I proceed to examine the issue *vis-à-vis* the material available on record before me, it would be appropriate to refer to the provisions of law applicable, which are alleged to have been violated by the Noticee and/ or are referred to in the present proceedings. The same are reproduced below for ease of reference:

SEBI Act, 1992

Registration of stock brokers, sub-brokers, share transfer agents, etc.

12.(3) The Board may, by order, suspend or cancel a certificate of registration in such manner as may be determined by regulations:

Provided that no order under this sub-section shall be made unless the person concerned has been given a reasonable opportunity of being heard.

Stock Brokers Regulations, 1992

Consideration of application for grant of registration.

5. The Board shall take into account for considering the grant of a certificate, all matters relating to trading, settling or dealing in securities and in particular the following, namely, whether the applicant,

(e) is a fit and proper person based on the criteria specified in Schedule II of the Securities and Exchange Board of India (Intermediaries) Regulations, 2008

Conditions of registration

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

(b) he shall abide by the rules, regulations and bye-laws of the stock exchange which are applicable to him;

…

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

Liability for action under the Securities and Exchange Board of India (Intermediaries) Regulations, 2008.

27. A stock broker shall be liable for any action as specified in Chapter V of the Securities and Exchange Board of India (Intermediaries)Regulations, 2008 including suspension or cancellation of his certificate of registration as a stock broker, if he —

(iv) has been found to be not a fit and proper person by the Board under these or any other regulations;

Intermediaries Regulations, 2008

SCHEDULE II

SECURITIES AND EXCHANGE BOARD OF INDIA (INTERMEDIARIES) REGULATIONS, 2008

[See regulation 7]

(1) The applicant or intermediary shall meet the criteria, as provided in the respective regulations applicable to such an applicant or intermediary including:

(a) the competence and capability in terms of infrastructure and manpower requirements; and

(b) the financial soundness, which includes meeting the net worth requirements.

(2) The 'fit and proper person' criteria shall apply to the following persons:

(a) the applicant or the intermediary;

(b) the principal officer, the directors or managing partners, the compliance officer and the key management persons by whatever name called; and

(c) the promoters or persons holding controlling interest or persons exercising control over the applicant or intermediary, directly or indirectly:

Provided that in case of an unlisted applicant or intermediary, any person holding twenty percent or more voting rights, irrespective of whether they hold controlling interest or exercise control, shall be required to fulfil the 'fit and proper person' criteria.

Explanation *–For the purpose of this sub-clause, the expressions "controlling interest" and "control" in case of an applicant or intermediary, shall be construed with reference to the respective regulations applicable to the applicant or intermediary.*

(3) For the purpose of determining as to whether any person is a 'fit and proper person', the Board may take into account any criteria as it deems fit, including but not limited to the following:

(a) integrity, honesty, ethical behaviour, reputation, fairness and character of the person;

(b) the person not incurring any of the following disqualifications:

(i) criminal complaint or information under section 154 of the Code of Criminal Procedure, 1973 (2 of 1974) has been filed against such person by the Board and which is pending;

(ii) charge sheet has been filed against such person by any enforcement agency in matters concerning economic offences and is pending;

(iii) an order of restraint, prohibition or debarment has been passed against such person by the Board or any other regulatory authority or enforcement agency in any matter concerning securities laws or financial markets and such order is in force;

(iv) recovery proceeding s have been initiated by the Board against such person and are pending;

(v) an order of conviction has been passed against such person by a court for any offence involving moral turpitude;

(vi) any winding up proceedings have been initiated or an order for winding up has been passed against such person;

(vii) such person has been declared insolvent and not discharged;

(viii) such person has been found to be of unsound mind by a court of competent jurisdiction and the finding is in force;

(ix) such person has been categorized as a wilful defaulter;

(x) such person has been declared a fugitive economic offender; or

(xi) any other disqualification as may be specified by the Board from time to time.

(4) Where any person has been declared as not 'fit and proper person' by an order of the Board, such a person shall not be eligible to apply for any registration during the period provided in the said order or for a period of five years from the date of effect of the order, if no such period is specified in the order.

(5) At the time of filing of an application for registration as an intermediary, if any Notice to show cause has been issued for proceedings under these regulations or under section 11(4) or section 11B of the Act against the applicant or any other person referred in clause (2), then such an application shall not be considered for grant of registration for a period of one year from the date of issuance of such Notice or until the conclusion of the proceedings, whichever is earlier.

(6) Any disqualification of an associate or group entity of the applicant or intermediary of the nature as referred in sub -clause (b) of clause (3), shall not have any bearing on the 'fit and proper person' criteria of the applicant or

intermediary unless the applicant or intermediary or any other person referred in clause (2), is also found to incur the same disqualification in the said matter: Provided that if any person as referred in sub-clause (b) of clause (2) fails to satisfy the 'fit and proper person' criteria, the intermediary shall replace such person within thirty days from the date of such disqualification failing which the 'fit and proper person' criteria may be invoked against the intermediary:

Provided further that if any person as referred in sub -clause (c) of clause (2) fails to satisfy the 'fit and proper person' criteria, the intermediary shall ensure that such person does not exercise any voting rights and that such person divests their holding within six months from the date of such disqualification failing which the 'fit and proper person' criteria may be invoked against such intermediary.

(7) The 'fit and proper person' criteria shall be applicable at the time of application of registration and during the continuity of registration and the intermediary shall ensure that the persons as referred in sub -clause s (b) and (c) of clause (2) comply with the 'fit and proper person' criteria."

Recommendation of action

26. (1) After considering the material available on record and the reply, if any, the designated authority may by way of a report, recommend the following measures, –

(i) disposing of the proceedings without any adverse action;

(ii) cancellation of the certificate of registration;

(iii) suspension of the certificate of registration for a specified period;

(iv) prohibition of the Noticee from taking up any new assignment or contract or launching a new scheme for such the period as may be specified;

(v) debarment of an officer of the Noticee from being employed or associated with any registered intermediary or other person associated with the securities market for such period as may be specified;

(vi) debarment of a branch or an office of the Noticee from carrying out activities for such period as may be specified;

(vii) issuance of a regulatory censure to the Noticee:

Provided that in respect of the same certificate of registration, not more than five regulatory censures under these regulations may be recommended to be issued, thereafter, the action as detailed in clause (ii) to (vi) of this sub-regulation may be considered.

Order

27. (5) After considering the facts and circumstances of the case, material on record and the written submission, if any, the competent authority shall endeavor to pass an appropriate order within one hundred and twenty days from the date of receipt of submissions under sub-regulation (2) or the date of personal hearing, whichever is later

7. Before proceeding further in the matter, I note that the Noticee, vide its letter dated August 14, 2023 has requested SEBI to keep the present proceedings in abeyance in light of the Order dated July 06, 2023 of Hon'ble Bombay High Court in the matter of *Venkataraman Rajamani and Ors. vs SEBI* in a batch of writ petitions. In this regard, it is pertinent to note that on perusal of the chargesheets filed by EOW in the NSEL matter, SEBI had noted that certain individuals, who were named in it, were also functioning as directors/ promoters/ MDs/CEOs in the associated broking firms of the commodity broking firms, who have been chargesheeted in the NSEL matter. Since such individuals, common to the commodity brokers and associated broking firms, had been chargesheeted by EOW in December, 2022, SEBI issued the impugned notices/communications dated June 19, 2023 to the associated broking firms seeking information on the manner of compliance of said associated broking firms with Clause 6 of Schedule II of the Intermediaries Regulations which provides that disqualification of an associate or group entity of the intermediary of the nature as referred in sub clause (b) of clause (3) shall not have any bearing on the 'fit and proper person' criteria of the intermediary unless the intermediary or any other person referred in Clause (2), is also found to incur the same disqualification in the said matter. The Proviso to the said Clause (6) however provides that if any person as referred in sub-clause (b) of clause (2) fails to satisfy the 'fit and proper person' criteria, the intermediary shall replace such person within thirty days from the date of such disqualification and that the intermediary shall also ensure that such person does not exercise any voting rights and also divests its holding within 6 months from the date of disqualification, failing which the 'fit and proper person' criteria may be invoked against the intermediary. In this background, after hearing brief arguments from both sides, Hon'ble Bombay High Court, vide the aforesaid Order, *inter alia*, directed as follows: -

"…. 2. Although we have heard the parties for some time, we accept Mr Dada's statement on behalf of SEBI that given the pendency of the matters before the Court and the challenges that are raised, SEBI is not presently insisting on compliance within 15 days with the requirements of paragraph 4 of the notice

at page 122 in Writ Petition (Lodging) No. 18014 of 2023. We note the statement. Mr Dada's statement is clearly on a without prejudice basis…."

Thus, it is clear that the subject matter of the said petitions has nothing to do with the issue under present proceedings which is solely to determine the fit and proper status of the Noticee. Accordingly, I do not find merit in the request raised by the Noticee vide its letter dated August 14, 2023.

8. Noticee has contended that there is an inordinate delay in initiating the present proceedings and issuance of the SCN against the Noticee. In this context, the Hon'ble Supreme Court in Adjudicating Officer, *Securities and Exchange Board of India v. Bhavesh Pabari* [1] observed that delay in issue of the SCNs itself would not exonerate the defaulters from the default. Reference may also be made to the order of the Hon'ble Supreme Court in the matter of *SEBI v. Sunil Krishna Khaitan and Ors*[2] on the aspect of delay and its impact on proceedings in the context of SEBI. The Hon'ble Supreme Court while referring to its earlier decision in the matter of *Bhavesh Pabari (supra)* held as follows:

> *"81. This Court in the judgment authored by one of us (Sanjiv Khanna, J.) in Bhavesh Pabari (supra) had examined the question of delay and laches in initiating proceedings under Chapter VI-A of the Act and the principle of law that when no limitation period is prescribed proceedings should be initiated within a reasonable time and what would be reasonable time would depend upon facts and circumstances of each case. In this regard, it was held as under:*
>
> > *"35. The Appellants have also contended that in the absence of any prescribed limitation period, SEBI should have issued show-cause notice within a reasonable time and there being a delay of about 8 years in issuance of show-cause notice in 2014, the proceedings should have been dropped. This contention was not raised before the adjudicating officer in the written submissions or the reply furnished. It is not clear whether this contention was argued before the Appellate Tribunal. There are judgments which hold that when the period of limitation is not prescribed, such power must be exercised within a reasonable time. What would be reasonable time, would depend upon the facts and circumstances of the case, nature of the default/statute, prejudice caused, whether the third-party rights had been created, etc.*

1 (2019) 5 SCC 90. Available at: https://main.sci.gov.in/supremecourt/2013/36291/36291_2013_Judgement_28-Feb-2019.pdf

2 Civil Appeal No. 8249 of 2013, decided on July 11, 2022. Availabale at: https://www.sebi.gov.in/enforcement/orders/jul-2022/judgment-of-the-hon-ble-supreme-court-in-civil-appeal-no-8249-of-2013-sebi-vs-sunil-krishna-khaitan-and-ors-_61342.html

The show-cause notice in the present case had specifically referred to the respective dates of default and the date of compliance, which was made between 30-8-2011 to 29-11-2011 (delay was between 927 days to 1897 days). Only upon compliance being made that the defaults had come to notice. In the aforesaid background, and so noticing the quantum of fine/penalty imposed, we do not find good ground and reason to interfere."

82. The directions given in the aforesaid quotation should not be understood as empowering the authorities/Board to initiate action at any time. In the absence of any period of time and limitation prescribed by the enactment, every authority is to exercise power within a reasonable period. What would be the reasonable period would depend upon facts of each case, such as whether the violation was hidden and camouflaged and thereby the Board or the authorities did not have any knowledge. Though, no hard and fast Rules can be laid down in this regard as determination of the question will depend on the facts of each case, the nature of the statute, the rights and liabilities thereunder and other consequences, including prejudice caused and whether third party rights have been created are relevant factors. Whenever a question with regard to inordinate delay in issuance of a show-cause notice is made, it is open to the noticee to contend that the show-cause notice is bad on the ground of delay and it is the duty of the authority/ officer to consider the question objectively, fairly and in a rational manner. There is public interest involved in not taking up and spending time on stale matters and, therefore, exercise of power, even when no time is specified, should be done within reasonable time. This prevents miscarriage of justice, misuse and abuse of the power as well as ensures that the violation of the provisions are checked and penalised without delay, thereby effectuating the purpose behind the enactment."

9. In view of the aforesaid decisions, it is clear that no specific limitation period has been provided in the SEBI Act but than even in the absence of a limitation period in the SEBI Act, the proceedings have to be initiated in a timely manner by the regulator. In the present matter, although the trades were executed in the year 2013, SEBI was granted the jurisdiction to regulate the commodities segment only in 2015. Pursuant thereto, given the magnitude of the NSEL scam and upon examination of all relevant records and after identifying the entities involved, a show cause notice was issued by the DA on September 25, 2018. It must also be noted that although the Noticee has raised the plea of delay, it has not stated the prejudice that has been caused to it, if any, on account of the delay. Accordingly, I am of the view that the plea regarding delay in initiation of the proceedings raised by the Noticee is not tenable.

10. The Noticee has vehemently contended that it has not been provided with inspection of all the documents sought by it. I note that Sub-regulations (3) and (4) of Regulation 25 of the Intermediaries Regulations specify that the copies of the documents "relied upon by SEBI" along with the extracts of relevant portions of the reports containing the findings arrived at in an inquiry, investigation or inspection, if any, shall be provided to the Noticee. In this regard, on perusal of the SCN, Enquiry Report and material/ information available on record, I find that Noticee was provided an opportunity to inspect the documents earlier on September 03, 2020 and recently on July 06, 2023. All the documents relied upon by SEBI and relevant for levelling charges against the Noticee have already been provided to the Noticee vide the Enquiry Report, SCN and Hearing Notice. I note that vide email dated July 07, 2023, the relevant details of the trade logs received from EOW which contained details of trades executed by the Noticee on NSEL during the year 2013 was also provided. Thus, I find no merit in these contentions of the Noticee in this regard.

11. Noticee has also contended that it was not provided with personal hearing before the DA even though there was no exemption/prohibition for grant of personal hearing by the DA under the Intermediaries Regulations. In this regard, I note that the DA had issued the show cause notice dated September 25, 2018 under the then existing Regulation 25(1) of the Intermediaries Regulations. Thereafter, the Enquiry Report was submitted on February 28, 2020. The Intermediaries Regulations were amended vide the SEBI (Intermediaries) (Amendment) Regulations, 2021, w.e.f. January 21, 2021. The amended Regulations now provide that the DA shall grant an opportunity of personal hearing and issue or cause to issue a notice scheduling a date for hearing. Thus, under the then existing Intermediaries Regulations prior to its amendment w.e.f. January 21, 2021, there was no legal requirement for providing the opportunity of personal hearing to the Noticee by the DA as contended by the Noticee. The Regulations specified granting of opportunity of personal hearing by the competent authority, which has been provided to and availed by the Noticee. Thus, this contention of the Noticee is not tenable and rejected.

12. As noted above, taking cognizance of the order passed by Hon'ble SAT dated June 09, 2022, in NSEL matters, a Hearing Notice dated November 10, 2022 was issued to the Noticee calling upon it to show cause as to why the following information/ material along with the Enquiry Report dated February 28, 2020 should not be considered against it for determining whether the Noticee satisfies 'fit and proper person' criteria as laid down under Schedule II of the Intermediaries Regulations:

    a. SEBI complaint dated September 24, 2018 filed with EOW;
    b. First Information Report dated September 28, 2018; and
    c. Amended Schedule II of the Intermediaries Regulations.

13. Noticee has contended that Regulation 27 of the Intermediaries Regulations does not provide for reliance on any other document or information which was not considered by the DA and in view of the additional documents and circumstances the matter ought to be remitted to the DA in terms of Regulation 27(3) of the Intermediaries Regulations. In this regard, I find it pertinent to refer to the following paragraph of Hon'ble SAT's Order dated June 09, 2022:

    "It will be open to the WTM to rely upon other material such as the complaint letters of NSEL, EOW report, EOW charge sheet, etc. provided such copies are provided to the brokers and opportunity is given to rebut the allegations. Such additional documents relied upon by the respondent should form part of the show cause notice for which purpose, it will be open to the WTM to issue a supplementary show cause notice...".

    Accordingly, in compliance of the order of Hon'ble SAT, additional documents were provided to the Noticee. Thus, in my view, the same cannot, in any manner, warrant the matter to be remitted to the DA. Thus, the submission of the Noticee in this regard are therefore rejected.

14. Before moving forward to test the fulfilment of the 'fit and proper' person criteria by the Noticee, on the basis of available material including the additional material

as detailed at paragraph 12 above, the background facts necessary for the present proceedings are narrated in brief, hereunder:

a. The Noticee is a commodity derivatives broker registered with SEBI having Registration No. INZ000076330.

b. NSEL was incorporated in May, 2005 as a Spot Exchange, *inter alia*, as an electronic exchange for trading in commodities. In exercise of powers conferred under Section 27 of the Forward Contracts (Regulation) Act, 1952 (hereinafter referred to as the **"FCRA"**), the Central Government vide its Exemption Notification granted an exemption to all forward contracts of one-day duration for the sale and purchase of commodities traded on the NSEL from operations of the provisions of the FCRA subject to certain conditions, *inter alia*, including *"no short sale by the members of the exchange shall be allowed"* and *"all outstanding positions of the trades at the end of the day shall result in delivery".*

c. In October 2008, NSEL commenced operations providing an electronic trading platform to its participants for spot trading of commodities, such as bullion, agricultural produce, metals, etc. It is observed that NSEL introduced the concept of 'paired contracts' in September 2009 which allowed buy and sell in same commodity through two different contracts at two different prices on the exchange platform wherein the investors could buy a short duration contract and sell a long duration contract and vice versa at the same time and at a pre-determined price. The trades for the Buy contract (T+2/ T+3) and the Sell contract (T+25/ T+36) used to happen on the NSEL on the same day at same time and at different prices, involving the same counterparties. The transactions were structured in a manner that buyer of the short duration contact always ended up making profits.

d. On February 06, 2012, FMC was appointed by the Department of Consumer Affairs, Government of India as the 'designated agency' as stipulated in one of the conditions specified under the said Exemption Notification, authorizing it to collect the trade data from NSEL and to examine the same for taking appropriate measures, if needed, to protect investors' interest. FMC had accordingly called for the trade data from NSEL in the specified reporting formats. After analysing the trade data received from NSEL, FMC passed

Order No. 4/5/2013-MKT-1/B dated December 17, 2013 in the matter ("**FMC Order**") wherein it was, *inter alia*, observed that 55 paired contracts offered for trade on the NSEL platform were in violation of the relevant provisions of the FCRA and that the condition of '*no short sale by members of the exchange shall be allowed',* specified in the Exemption Notification*,* was not being complied by NSEL and its members.

15. I note that FMC was a statutory body set up under the FCRA and its functions were enumerated under section 4 of the Act. FCRA regulated forward contracts in notified goods entered into between the members of a recognised association or through or with any such member. An association recognised under the FCRA was empowered to make rules and bye-laws for the regulation of forward contracts subject to approval of the Central Government/FMC. Such an association concerned with the regulation and control of business relating to forward contracts was also required to obtain a certificate of registration from FMC, under FCRA. I note that FMC was having jurisdiction only on the associations recognised or registered under the FCRA or any member of such association. NSEL was not an association recognised under section 6 of FCRA nor was it an association registered under section 14A of FCRA, which provided that –

"No association concerned with the regulation and control of business relating to forward contracts shall, after the commencement of the Forward Contracts (Regulation) Amendment Act, 1960 (62 of 1960) carry on such business except under, and in accordance with the conditions of a certificate of registration granted under this Act by the Commission."

16. Section 27 of the FCRA empowered the Central Government to exempt any contract or class of contracts from the operation of all or any of the provisions of the Act. In exercise of the powers conferred under Section 27 of the FCRA, the Central Government, vide the Exemption Notification, had granted exemption to one-day forward contracts traded on NSEL from the operation of all provisions of FCRA, subject to conditions mentioned in the said Exemption Notification. Subsequently, the Central Government has issued notifications on February 06,

2012 and August 06, 2013, in partial modification of this notification dated June 05, 2007, by way of amending or inserting new conditions to the original notification, thereby assigning specific responsibility to FMC with respect to NSEL. Recognised associations were empowered to make rules and bye-laws under FCRA which would be approved by the Central Government/ FMC. However, NSEL was neither a registered nor a recognised association/ Exchange under FCRA and the bye-laws of NSEL were not reviewed or regulated or monitored by any authority.

17. I note that prior to the merger of FMC with SEBI on September 28, 2015, the Noticee was not required to be registered with either FMC or any other regulatory authority under the FCRA. The Parliament, noticing that the intermediaries dealing with commodities derivatives market were not required to be registered under FCRA and were not under control of any competent authority, rectified the same through the Finance Act, 2015, as notified on May 14, 2015, by bringing them under the regulatory supervision of SEBI. With regard to the aforesaid, the Hon'ble Bombay High Court while dealing with the Writ Petition Nos. 3262, 3266, 3294 and 3295 of 2018 in the matter of *Anand Rathi Commodities Limited*, *Motilal Oswal Commodities Broker Private Limited*, *Geofin Comtrade Limited* and *IIFL Commodities Limited vs. SEBI,* vide its Order dated October 04, 2018, observed the following:

> *"It is not in dispute that prior to the coming into effect of the Finance Act, 2015, the intermediaries dealing with the commodity derivatives were not required to be registered under any of the provisions of law including the FCR Act. We find that the said mischief was Noticed by the Parliament. As such, by virtue of the Finance Act, 2015, the said intermediaries dealing with commodity derivatives have been brought under the control of SEBI. We find that the reason as to why by Finance Act, 2015, the said intermediaries were brought under the control of SEBI appears to be that the Parliament found that the activities of intermediaries dealing in commodity derivatives should not remain uncontrolled and they should be brought under the control of competent authority".*

18. I further note that the provisions in the Finance Act, 2015 effecting the merger of FMC with SEBI in September, 2015 do not, *prima facie*, confer any power on SEBI to take charge, deal, inquire and resolve NSEL settlement crisis that broke

out in 2013. Pursuant to repeal of FCRA and dissolution of FMC in terms of Section 131 of Finance Act, 2015, all recognised associations under the FCRA became deemed recognised stock exchanges under the Securities Contracts (Regulation) Act, 1956 (hereinafter referred to as the "SCRA"). NSEL was not a recognised association under FCRA, therefore, a question regarding NSEL falling under the regulatory jurisdiction of SEBI does not arise.

19. I note that pursuant to the merger of FMC with SEBI, a commodity derivatives broker was mandatorily required to obtain a certificate of registration from SEBI in case it sought to remain associated with the securities market as a commodity derivatives broker. The Finance Act, 2015, *inter alia*, conferred the powers to SEBI to regulate commodity derivatives brokers, which included their registration as commodity derivatives broker with SEBI. In this regard, vide Section 131B of the Finance Act, 2015, a transitory period of 3 months was provided to all the intermediaries which were associated with the commodity derivatives market under the erstwhile FCRA to continue to deal in commodity derivatives as a commodity derivatives broker, provided it made an application of registration to the SEBI within 3 months from September 28, 2015. Accordingly, the Noticee applied for a certificate of registration and was registered as a broker with effect from December 22, 2015 and since then it has been acting as a market intermediary registered with SEBI.

20. The Noticee has contended that the SCN is bad in law since it seeks to take action for trades executed at a time when the Noticee was governed by the FMC and the SEBI regulations were not applicable to the members of NSEL at that relevant time. I note that the issue under consideration in the present proceedings is limited to the determination of "*fit and proper"* status of the Noticee under the Intermediaries Regulations. It is a settled position of law that SEBI has statutory authority to determine the "*fit and proper"* status of the intermediaries registered with it. Since the Noticee is an intermediary registered with SEBI, I am of the considered view that SEBI is within its jurisdiction to determine the "*fit and proper"* status of the Noticee.

21. The Noticee has submitted that the proceedings by SEBI are vitiated and not maintainable since under the erstwhile FCRA, the power to investigate was with the police and not by SEBI. Further, Ministry of Finance vide letter dated November 20, 2015 had advised that SEBI is not expected to deal with the matters which were not dealt by erstwhile FMC. It is matter of record that FMC had not initiated any action against the Noticee, thus SEBI is not expected to take upon itself any regulatory function with respect to spot market. In this regard, I note that the power of SEBI to investigate/ inquire into the alleged violation of FCRA flows from the Finance Act, 2015, which amended the provisions of FCRA. Section 29A of FCRA, as inserted by the Finance Act, 2015 provides as under–

"(1) The Forward Contracts (Regulation) Act, 1952 is hereby repealed.
(2) On and from the date of repeal of Forward Contracts Act–
(a)….
(b)….
(c)….
(d)….
(e) a fresh proceeding related to an offence under the Forward Contracts Act, may be initiated by the Security Board under that Act within a period of three years from the date on which that Act is repealed and be proceeded with as if that Act had not been repealed;
(f) no court shall take cognizance of any offence under the Forward Contracts Act from the date on which that Act is repealed, except as provided in clause (d) and (e);
(g) clause (d), (e), (f) shall not be held to or affect the general application of section 6 of the General Clauses Act, 1897 with regard to the effect of repeal to matters not covered under these sub-sections."

22. I note that the aforesaid provision empowers SEBI to initiate a fresh proceeding with respect to the offences within a period of three years from the date on which FCRA is repealed. Thus, pursuant to the merger of FMC with SEBI, SEBI stepped into the shoes of FMC and was well within its powers to initiate proceedings under Chapter V of FCRA i.e., filing of the criminal complaint to the EOW. I note from the complaint dated September 24, 2018 filed by SEBI that EOW was requested to take appropriate action under Sections 20 and 21 and other provisions of FCRA against the brokers/ members of NSEL and other persons mentioned in the complaint. However, it is relevant to mention here that the aforesaid proceedings are different from the proceedings before me.

23. It is noted that the present proceedings pertain to adjudging the 'fit and proper person' status specified in the Broker Regulations and the Intermediaries Regulations in light of the activities undertaken by the Noticee on the NSEL platform and consequent action taken by FMC and SEBI, i.e., filing of the criminal complaint to EOW under Section 154 of the Code of Criminal Procedure, 1973 ("CrPC"). I note that in terms of Regulation 5(e) of the Stock Brokers Regulations, every applicant/ stock broker at the time of seeking registration, and thereafter, throughout the time it holds a valid certificate of registration, has to satisfy the "fit and proper person" criteria specified in Schedule II of the Intermediaries Regulations. I note that the Enquiry Report proceeds on the basis that the past conduct of the Noticee in facilitating access to the "paired contracts" traded on NSEL calls into question the compliance of the Noticee with 'fit and proper person' criteria. Further, SEBI while examining the compliance of an applicant, or even a registered intermediary, with the 'fit and proper person' criteria can take into consideration not just contravention of the provisions of securities laws, but also the general conduct of the Noticee which may have a bearing on its functioning as a registered intermediary. The 'fit and proper' criteria including the amended criteria must be satisfied by the Noticee, at the time of making application of registration under the Stock Brokers Regulations as well as during the continuance of the registration once granted. Thus, it is well within the jurisdiction and powers of SEBI to adjudge the said 'fit and proper' status of the market intermediaries in the interest of securities market.

24. Before moving forward to consider the matter on merits, it would be appropriate to look at the background of NSEL and understand the nature of the 'paired contracts' that were offered on NSEL which ultimately is the cause/ genesis of the current proceedings.

25. From the perusal of the FMC Order in respect of the 'paired contracts', which were traded on the NSEL platform during the relevant period, I note that the FMC had, *inter alia*, observed that the following conditions stipulated in the Exemption Notification were violated:

a. Short Sale

NSEL had not made it mandatory for the seller to deposit goods in its warehouse before taking a sell position. Hence, the condition of "*no short sale by members of the NSEL shall be allowed"* was not being met by the NSEL and its trading/clearing members who traded in the 'paired contracts' during the relevant period.

b. Contracts with Settlement Period going beyond 11 days

Some of the contracts offered for trade on the NSEL had settlement periods exceeding 11 days and therefore, such contracts were "non-transferable specific delivery" contracts under the FCRA. As per the FCRA, the "ready delivery contracts" were required to be settled within 11 days of the trade and hence, the contracts traded on the NSEL, which provided settlement schedule for a period exceeding 11 days were not allowed and were in violation of Exemption Notification.

26. In this context, I note that NSEL was granted conditional exemption from the provisions of the FCRA by the Department of Consumer Affairs, Ministry of Consumer Affairs (hereinafter referred to as the **"MCA"**), Food and Public Distribution, Government of India, vide Gazette Notification No. S0906(E) dated June 05, 2007, in exercise of the powers conferred under Section 27 of the FCRA, for forward contracts for sale and purchase of the commodities of one–day duration traded on NSEL subject to certain conditions which*, inter alia*, included that 'no short sale by members of the NSEL shall be allowed' and that all '*outstanding positions of the trade at the end of the day shall result in delivery'*. It was also stipulated that all information or returns relating to the trade as and when asked for shall be provided to the Central Government or its designated agency. The spot exchanges were envisaged as a platform for providing transparent and secure trading in commodities with a view to boost the agriculture sector in the country. Thereafter, NSEL commenced operations in October 2008.

27. The Noticee has contended that all the trades were executed by it in accordance with the rules and regulations specified by the NSEL and NSEL had been openly allowing trading in a variety of commodities details whereof were being regularly reported to the FMC. It has also submitted that the first leg of the alleged paired contracts was always a "purchase" and thus, there is no question of short sale and it had fulfilled its trading obligation on execution of buy and sell contracts independently and had made full payment of consideration of buy contract. In this regard, it is observed that NSEL was given permission to setup as a spot exchange for trading in commodities. It was essentially meant to only offer forward contracts having one-day duration as per the Exemption Notification. In its order, FMC had observed that the 55 contracts offered for trade on the NSEL were with settlement periods exceeding 11 days and all such contracts traded on the NSEL were in violation of provisions of FCRA. I note from the FMC Order that under the FCRA, a "forward contract" is defined as a *"contract for delivery of goods and which is not a ready delivery contract"*. A 'ready delivery contract' is defined as *"a contract which provides for the delivery of goods and the payment of a price therefor, either immediately or within such period not exceeding eleven days"*. Given the said definition contained in the FCRA, FMC was of the view that all the contracts traded on the NSEL which provided settlement schedule exceeding 11 days were treated as Non-Transferable Specific Delivery contracts. It is, therefore, seen that even though MCA had stipulated in the Exemption Notification that only contracts of one-day duration were permitted to be offered on the NSEL, the FMC, in its order, relying on the definition of the "forward contract" under FCRA held that the NSEL was allowed to only trade in one-day forward contracts and was obliged to ensure delivery and settlement within 11 days. However, what is beyond doubt is that the NSEL had permitted 55 contracts of various commodities having duration longer than 11 days and these contracts were in contravention of the exemption granted to NSEL.

28. At this stage, it is also pertinent to refer to the judgment of the Hon'ble Supreme Court of India passed in the matter of *63 Moons Technologies Ltd. (formerly known as Financial Technologies India Ltd.) & Ors. vs. Union of India & Others*

(Civil Appeal No. 4476 of 2019 decided on April 30, 2019) (hereinafter referred to as the **"merger petition"**), wherein it was, *inter alia*, held that:

> *"55.3 We have seen that neither FTIL nor NSEL has denied the fact that 'paired contracts' in commodities were going on, and by April to July, 2013, 99% (and excluding E-series contracts), at least 46% of the turnover of NSEL was made up of such 'paired contracts'. There is no doubt that such Paired Contracts were, in fact, financing transactions which were distinct from sale and purchase transactions in commodities and were, thus, in breach of both the exemptions granted to NSEL, and the FCRA".*

29. Further, I note that in the judgment dated April 22, 2022 passed by the Hon'ble Supreme Court in the matter of the ***State of Maharashtra vs. 63 Moons Technologies Ltd.*** (Civil Appeal No. 2748-49 of 2022) (hereinafter referred to as the **"MPID matter"**), the Hon'ble Supreme Court while drawing reference to the representations made by NSEL in respect of the paired contracts, *inter alia*, held that:

> *"The above representation indicates that 'paired contracts' were designed as a unique trading opportunity by NSEL under which a trader would, for instance, purchase a T+2 contract (with a pay-in obligation on T+2) and would simultaneously sell a T+25 contract (with a pay-out of funds on T+25). The price differential between the two settlement dates was represented to offer an annualized return of about 16%. NSEL categorically represented that all trades were backed by collaterals in the form of stocks and its management activities included selection, accreditation, quality testing, fumigation and insurance. Therefore, NSEL represented that on receiving money and commodities, the members would receive assured returns and a service. Though NSEL has been receiving deposits, it has failed to provide services as promised against the deposits and has failed return the deposits on demand. Therefore, the State of Maharashtra was justified in issuing the attachment notifications under Section 4 of the MPID Act."*

30. Thus, I note that the Hon'ble Supreme Court has already described the nature of the 'paired contracts' offered on the NSEL platform. In the merger petition (*63 Moons Technologies Ltd. vs. UOI*), it was held that these contracts were in the nature of financing transactions. In the MPID matter (*The State of Maharashtra vs. 63 Moons Technologies Ltd.*), the Hon'ble Supreme Court held that such transactions come within the definition of 'deposits' under the MPID Act. The Hon'ble Supreme Court in the MPID matter, has extensively referred to the

claims made on the website of the NSEL and the contents of the publicity material and other investor resources. The Hon'ble Supreme Court has also observed that NSEL was advertising assured and uniform return of 16% p.a. for the 'paired contracts' traded on its platform where the return offered was same across the commodities. The return remained the same irrespective of the duration of the contract. In the said Order, the Hon'ble Supreme Court has also depicted certain examples of 'paired contracts', which offered assured returns. For example, a T+2 and T+25 paired contract in steel had the same offered return as a T+5 and T+35 paired contract in castor oil. The 'paired contracts' were being marketed as an alternative to fixed deposits. In view of the above, I note that the FMC Order and both the judgments of the Hon'ble Supreme Court discuss in detail that, NSEL was permitting short sales, i.e., permitting sellers to offer contract for sale of commodities on its platform without ensuring that requisite amount of commodity is available in the warehouse.

31. In view of the above discussion, I do not find any merit in the arguments of the Noticees regarding execution of trades being in accordance with the rules and regulations specified by the NSEL, NSEL allowing trading in a variety of commodities details whereof were being regularly reported to the FMC, first leg of the alleged paired contracts not leading to any question of short sale, etc. which have been noted earlier.

32. Another contention of the Noticee is that in view of the order of Hon'ble SAT dated June 09, 2022, various orders/ judgments/ reports passed/ issued by various regulatory authorities as referred in the Enquiry Report cannot be considered and observations in respect of the same should be quashed and set aside. The Enquiry Report dated February 28, 2020 was prepared on the basis of material available on record at that point of time, much before the order of Hon'ble SAT dated June 09, 2022. It is noted that in the present proceedings, no reliance has been placed on any of the grounds which have been specifically rejected by SAT. Thus the contention of the Noticee in this regard is misplaced and is hence rejected.

33. As regards, the contention of the Noticee that no adverse remarks/red flags were raised against various agencies like MMTC, FCI, NAFED, etc. who had executed trades as clients on the NSEL platform and who were also purported to be closely associated with NSEL and that its dealings on the NSEL trading platform should also be considered on similar lines, I note that SEBI had passed an order dated August 02, 2023 against MMTC Limited in the matter of NSEL and cancelled its certificate of registration as a commodity broker for its role and involvement in the facilitation/trading in the paired contracts on the NSEL platform. I also note that proceedings have been proposed and initiated against several other entities based on the trades executed by them in the paired contracts on the NSEL platform and the accompanying facts and circumstances of their respective cases, solely relying on the material available on record. Since the Noticee was one such entity that had facilitated the trading in paired contracts on behalf of its client, the present proceedings have been initiated against it. The extent of the role of the Noticee has been clearly brought out in the SCN issued to it and as a quasi-judicial authority, the issue before me is to adjudicate the gravity of the allegations in the SCNs and arrive at a finding. Thus, the contention of the Noticee is liable to be rejected.

34. In so far as the trades of the Noticee on the platform of NSEL are concerned, I note that the DA in the Enquiry Report has observed that the Noticee had traded on NSEL in contracts, STLTMTKUR2 and STLTMTKUR25 on March 08, 2013. I note that with the SCN, the Noticee was provided with trade logs received by SEBI from EOW. Further, vide email dated July 07, 2023, the trading details were again shared with the Noticee. On perusal of the trade details it is observed that the Noticee had on January 28, 2013 and March 08, 2013 executed paired contracts on behalf of one of its client i.e. Mr. Peddi Govinda Rao. The Noticee has admitted to the said fact and further stated that it had also paid VAT as applicable for the physical delivery of the commodity viz. ‘Steel TMT Bars’ and have also paid warehousing charges. The Noticee has also submitted an affidavit from the said client *inter alia* stating that he is a well-informed investor and does his own research and analysis and that he only carried out the trades in paired contracts and invested his own money. Thus, it is clear that the Noticee had

executed two paired contracts in the year 2013 albeit only for one of its client. Further, the fact that the client demanded such access to the '*paired contracts'* after doing its own research and after investing own money or that it holds no grievance with the Noticee who executed the contracts without soliciting, does not lessen the extent of its obligations cast on the Noticee.

35. Considering the deliberations and discussions recorded above and the submissions of the Noticee, the moot question is whether the Noticee facilitated transactions in 'paired contracts' for its client under a bonafide belief that such transactions were actually spot contracts in commodities. Or, can it be said that the very fact that 'paired contracts' were offered meant that NSEL was offering contracts which were not resulting in compulsory delivery and, therefore, the Noticee should have been aware that such a product was far removed from the spot trading in commodities which was permitted on NSEL's platform.

36. NSEL itself was advertising such contracts as an alternative to fixed deposits and an annualized return of about 16% was offered across all commodities, irrespective of the nature of the contract or the duration. Also, these contracts were structured in a manner which ensured that the buyer always made pre-determined profits.

37. In the undeniable background that there was a settlement default at NSEL, and that there were enough red flags which should have alerted the Noticee when these products were first offered by NSEL. With the material on record, it is further clear that any prudent person (including the Noticee) would have come to the conclusion that what was being offered were not spot contract in commodities and rather had trappings of a financial product which offered fixed and assured returns, as has been already observed by the Hon'ble Supreme Court in the *State of Maharashtra vs. 63 Moons Technologies Ltd*. The Noticee was expected to do due diligence on the products which it offered for trading to its client. An assumption as to the legality of 'paired contracts' clearly shows that the Noticee failed to do adequate due diligence. The Notification regarding approval of contracts permitted on NSEL was in public domain. Thus, I find that Noticee failed

to perform basic due diligence of the contracts offered vis-a-vis the conditions specified in the aforesaid Notification.

38. Another argument raised by the Noticee that while granting registration to it, SEBI was fully aware that it had carried out the trades in alleged paired contracts and therefore the principles of res judicata would apply. I note that principle of *res judicata* as provided under Section 11 of the Code of Civil Procedure, 1908 provides that *no Court shall try any suit or issue in which the matter directly and substantially in issue has been directly and substantially in issue in a former suit between the same parties, or between parties under whom they or any of them claim, litigating under the same title, in a Court competent to try such subsequent suit or the suit in which such issue has been subsequently raised, and has been heard and finally decided by such Court.* Thus, if a suit is filed for a cause of action and the dispute is resolved or judged by the competent court within its jurisdiction then the subsequent suit filed for the same cause of action is barred by the principle of *res judicata*. In the present proceedings, the issue of fit and proper status of the Noticee has not been decided by SEBI earlier but is under consideration in the present proceedings. Thus, the issue of applicability of res judicata does not arise and the contention of the Noticee is misconceived.

39. I note that for the client, the face of NSEL and the 'paired contracts' was the Noticee itself and the 'paired contracts' could not have been executed without the actions and facilitation of the Noticee. The execution of the trades in ‘paired contracts’ by the Noticee shows the participation of the Noticee in the said scheme perpetrated by NSEL to facilitate trading in ‘paired contracts’ that were not permitted under the Exemption Notification and were purely financial contracts promising assured returns under the garb of spot trading in commodities. Therefore, the Noticee by its conduct and as a member of NSEL has acted as an instrument of NSEL in promoting and dealing in ‘paired contracts’ which were in the nature of financing transactions (as held by the Hon’ble Supreme Court of India referred *supra*). The Noticee, by providing access for taking exposure to ‘paired contracts’ has exposed its client to the risk involved in trading in a product that did not have regulatory approval, thereby raising doubts

on the competence of the Noticee to act as a registered Securities Market intermediary.

40. Having noted that the Noticee has traded in 'paired contracts' for its client, I now proceed to examine the allegations levelled against the Noticee in the SCN and the Hearing Notice. It is noted that the main allegation against the Noticee, as levelled in the SCN, is that by facilitating the trading in 'paired contracts' on NSEL platform during the relevant period as a Trading Member/ Clearing Member, the continuance of the registration of the Noticee as a broker is detrimental to the interest of the Securities Market and the Noticee is no longer a 'fit and proper person' for holding the certificate of registration as a broker in the Securities Market, which is one of the conditions for continuance of registration as specified in regulation 5(e) of the Stock Brokers Regulations read with Schedule II of the Intermediaries Regulations as applicable at the relevant time. Subsequently, SEBI, on the basis of certain documents/material such as SEBI's Complaint dated September 24, 2018 and FIR dated September 28, 2018 as provided to the Noticee vide Hearing Notice, further alleged that in light of the aforesaid documents as well as observations against the Noticee in the Enquiry Report, the Noticee is not a 'fit and proper person' for holding the certificate of registration. I note that regulation 5(e) of the Stock Brokers Regulations provides that for the purpose of grant of Certificate of Registration, the applicant has to be a 'fit and proper person' in terms of Schedule II of the Intermediaries Regulations. I further note that the 'fit and proper person' criteria specified in Schedule II of the SEBI (Intermediaries) Regulations, 2008, was amended vide SEBI (Intermediaries) (Third Amendment) Regulations, 2021 with effect from November 17, 2021.

41. In order to continue as a SEBI registered intermediary, the Noticee is, *inter alia*, required to satisfy the conditions of eligibility, which included 'fit and proper person' criteria. The above condition to be a fit and proper person is a preliminary condition applicable at the time of seeking registration and also during the continuance of such registration. As and when the 'fit and proper' criteria changes, the Noticee will be required to comply with the revised criteria, and in

this instance, criteria were revised vide the amendments in November 2021. It is noted that parameters provided under paragraph 3(b) of the amended criteria of Schedule II of the Intermediaries Regulations lay down a list of disqualifications which, *inter alia*, include the following:

> *"(3) For the purpose of determining as to whether any person is a 'fit and proper person', the Board may take into account any criteria as it deems fit, including but not limited to the following:*
>
> *(b) the person not incurring any of the following disqualifications:*
>
> *(i) criminal complaint or information under section 154 of the Code of Criminal Procedure, 1973 (2 of 1974) has been filed against such person by the Board and which is pending;"*

42. From the records, I note that SEBI has filed a complaint with EOW Mumbai on September 24, 2018, against brokers who facilitated access to *'paired contracts'* traded on NSEL, including the Noticee. On the basis of this complaint, FIR dated September 28, 2018, was registered with the MIDC Police Station, Mumbai, against the Noticee. I note that the Noticee is holding a certificate of registration granted by SEBI. In order to continue to hold such Certificate of Registration from SEBI, the Noticee is also required to satisfy the conditions of eligibility, which, *inter alia*, included, continuance of its status as a '*fit and proper person*'. The above condition to be *fit and proper* person is not a one-time condition applicable only at the time of seeking registration. Rather, the provisions governing the criteria show that this is a condition which each and every registered intermediary is required to fulfil on a continuous basis as long as the entity remains associated with the Securities Market as a registered intermediary.

43. The scope of the instant proceeding is not to analyse the actual impact and consequences of the conduct of the Noticee but to examine as to whether or not, the Noticee has acted in a manner expected of a market intermediary and the answer to the same manifestly goes against the Noticee. The fact that is undeniably clear before me is that the involvement of the Noticee in facilitation of trading in 'paired contracts' on NSEL is certainly a conduct which was not permitted by the Exemption Notification nor by any of the applicable provisions of the FCRA.

44. As discussed above, the Noticee has facilitated its client to trade in 'paired contracts'. As the paired contracts were violative of the conditions stipulated in the Exemption Notification, a complaint was filed by SEBI with EOW on September 24, 2018, against the brokers who participated/ facilitated access to 'paired contracts' traded on NSEL, including the Noticee within the time limit, as specified under section 29A(2)(e) of the FCRA. On the basis of the said complaint of SEBI, FIR dated September 28, 2018 was registered with MIDC Police Station, Mumbai.

45. The Noticee has also submitted that Schedule II of the Intermediaries Regulations was amended with effect from November 17, 2021 and the same cannot be made applicable retrospectively as the FIR against the Noticee was filed in the year 2018. In this regard, it is pertinent to note that the criteria of '*fit and proper person*', is an ongoing requirement throughout the period during which the Noticee remains operational in the Securities Market as a registered intermediary. In case, pursuant to the grant of registration by SEBI, any evidence comes to the notice of SEBI that casts a doubt on the integrity, reputation and character of the registered intermediary, SEBI is well within its powers to examine the '*fit and proper person*' status of such entity based on various parameters. Therefore, even if the Noticee was found to have fulfilled the '*fit and proper person*' criteria when SEBI granted it the certificate of registration in 2016, such an intermediary can still be assessed on being fit and proper at a later date. Furthermore, as and when the '*fit and proper person*' criteria changes, the Noticee will be required to comply with the revised criteria, and in the instant case, criteria as revised vide the amendment in November, 2021. It is noted that parameters provided under Clause 3(b) of the amended criteria of Schedule II of the Intermediaries Regulations lay down a list of disqualifications which includes the disqualification provided in Clause3(b)(i) under the amended Schedule II of the Intermediaries Regulations in so far as an FIR against the Noticee under section 154 of CrPC has been registered with the MIDC Police Station, Mumbai and the same is subsisting/pending as on date. Further, it is also not the case of the Noticee that the aforesaid FIR is either stayed or quashed

by any competent court qua the Noticee or otherwise. It is, therefore, noted that the Noticee attracts the disqualification provided in Clause 3(b)(i) of the Schedule II of the Intermediaries Regulations.

46. At this juncture, I deem it appropriate to deal with the submission of the Noticee that FIR cannot be taken into account as it is only a preliminary document and SEBI cannot adjudge its own allegations, pending outcome of its own complaint/FIR and the Noticee is not named in the chargesheet. I note that being a '*fit and proper*' person is a continuing '*eligibility criteria*'/ statutory requirement, which must be satisfied by the Noticee including the amended criteria, at all times. I am of the considered view that the due presumption on the constitutional and legal validity of the said amended Schedule II of the Intermediaries Regulations holds the field which is binding upon SEBI, and arguments to the contrary are not maintainable. Besides, no material has been brought on record by the Noticee to dispute the fact that the said FIR subsists as on date. In view of the above, I am not inclined to accept the submissions put forth by the Noticee in this context.

47. Given the above, I am constrained to conclude that the Noticee facilitated its client to access a product~~,~~ which was not permitted to trade. The same raises serious questions on the ability of the Noticee to conduct proper and effective due diligence regarding the product itself. By its failure to disassociate itself from, and to facilitate the participation in the said paired contracts, the Noticee failed to act with due diligence.

48. The Noticee has also submitted that the alleged paired contracts were launched by NSEL as per their Bye laws and with the permission of FMC and, thus, a trading member cannot be held liable for the wrong contracts introduced by NSEL. In this regard, I am of the view that, the principle of *'ignorantia juris non excusat'* or *'ignorantia legis neminem excusat'* or *'ignorance of law is no excuse'* becomes applicable in the situation, since trading in 'paired contracts' was in violation of the Exemption Notification and ignorance of the conditions of the said Exemption Notification cannot be claimed. As held by the Hon'ble Supreme Court, the 'paired contracts' were nothing but financing transactions which were

portrayed as spot contracts in commodities. Thus, I am not inclined to accept the submission of the Noticee in this regard.

49. In the context of Securities Market, I note that the role of a registered intermediary including a broker is not only sensitive and predominantly fiduciary in nature but also demands from it honesty, transparency, fairness and integrity which are essentially the hallmarks of such market intermediaries. Given the fact that one of the avowed objects of the SEBI Act is the protection of interest of investors apart from promotion and development of the Securities Market, the legislature through enactment, empowers SEBI to grant registration to several class of entities including brokers, which are not only required to act as an intermediary simplicitor, i.e., a bridge or a connector between the markets and investors, but also have a very important role to play in creating an ecosystem of trust and fairness so as to provide a fair and secure market to the investors and any deviation from the above noted objective could have a cascading adverse impact on the development of the Securities Market and interests of investors. Thus, undisputedly a broker is obligated to act in a transparent manner and comply with all applicable regulatory requirements which are in the best interests of its clients and which will uphold the integrity of the Securities Market.

50. Given the above discussions and deliberations, I conclude that the act of the Noticee in providing access to its client to participate in a product, which was not permitted to trade raises serious questions on the ability of the Noticee to conduct proper and effective due diligence regarding the said product itself. Further, as per findings recorded in earlier paragraphs, the Noticee attracts the disqualification provided in Clause 3(b)(i) under the amended Schedule II of the Intermediaries Regulations in view of the FIR filed against the Noticee which is pending as on date. Further, it is also not the case of the Noticee that said FIR is either stayed or quashed by any competent court *qua* the Noticee or otherwise. In view of the above, I hold that the Noticee does not satisfy the '*fit and proper person*' criteria specified in Schedule II of the Intermediaries Regulations.

Consideration of DA's recommendation:

51. The DA in the Enquiry Report, after determining that the Noticee is not "fit and proper", has recommended that the certificate of registration of the Noticee be cancelled.

52. As discussed in the preceding paragraphs, the facts and circumstances in the instant matter lead to the conclusion that the Noticee is not a "fit and proper" person. Once an entity has been declared to be not "fit and proper", in the interest of securities market, it should not be allowed to continue to act as an intermediary till the time it does not regain its "fit and proper" status. In this context, it is pertinent to mention that in several scenarios, a defect which is the reason for holding an intermediary not "fit and proper" is curable at the hands of the intermediary, while in certain scenarios, it is not.

53. In the present case, the Noticee has been found to be not 'fit and proper" for the reason that its conduct has been found wanting because of the Noticee's involvement in trading of "paired contracts" on the NSEL platform for one of its client and also for the reason that in that regard, a FIR dated September 28, 2018 has been registered by EOW, which is subsisting as on date.

54. Schedule II of the Intermediaries Regulations, in clause 4 provides that "*Where any person has been declared as not 'fit and proper person' by an order of the Board, such a person shall not be eligible to apply for any registration during the period provided in the said order or for a period of five years from the date of effect of the order, if no such period is specified in the order*". This clause, in my view, covers scenarios of 'cancelation' or 'suspension' of the certificate of registration of the intermediary.

55. Thus, the Intermediaries Regulations envisage deeming time limit (of 5 years) or specification of a time limit by the deciding authority, within which the intermediary can cure the defects which led to determination of its status, if the same can be done at its end. The said specification of period also serves as a reformative direction against the intermediary.

56. Considering the above, in the instant case, having held that the Noticee is not "fit and proper", the question for determination is what would be the appropriate direction in the given facts and circumstances. Noticee has submitted that it had traded in two paired contracts for only one of its client. I note that being a commodity broker and a member of MCX and NCDEX, Noticee ought to have been aware of the exemption granted to NSEL by the Central Government under the FCRA which exempted one-day forward contracts traded on NSEL from the operation of all provisions of FCRA. However, I deem it fit to note that given the frequency and the fact that the Noticee traded for only one client, the risk associated with the trading in paired contracts was limited to only that client.

57. The DA has recommended cancellation of the certificate of registration of the Noticee. However, given the fact that the Noticee participated in two paired contracts in the year 2013 and that too only for one client, I am of the considered view that a direction of prohibiting the Noticee from trading in proprietary capacity and taking up any new clients for a period of fifteen (15) days or till the time the FIR ceases to be "pending", would be proportionate and more appropriate in the present case and would meet the ends of justice.

Order:

58. In view of the foregoing discussions and deliberations, I, in exercise of powers conferred upon me under Section 12(3) and Section 19 of the SEBI Act, 1992 read with Regulation 27 of the Intermediaries Regulations, prohibit the Noticee i.e. Steel City Commodities Private Limited bearing Certificate of Registration (bearing No. INZ000076330) from trading in proprietary capacity and taking up any new clients for a period of fifteen (15) days from the date of this Order or till the FIR filed against the Noticee by EOW ceases to be pending or the Noticee is discharged or acquitted by a Court in relation to the FIR, whichever is later.

59. The Noticee shall, after receipt of this order, immediately inform its existing clients, if any, about the aforesaid direction.

60. This Order shall come into force with immediate effect.

61. The above Order is without prejudice to the proceedings pending in pursuance of the criminal complaint filed by SEBI in the matter of trading on NSEL and/or any proceedings pending before any authority in respect of similar matter concerning the Noticee or other relevant persons.

62. A copy of this order shall be served upon the Noticee and the recognized Market Infrastructure Institutions for necessary compliance.

Sd/-

Place: Mumbai
Date: December 22, 2023

AMARJEET SINGH
WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA