

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

UNDER SECTION 12(3) AND SECTION 19 OF SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 READ WITH REGULATION 27 OF SECURITIES AND EXCHANGE BOARD OF INDIA (INTERMEDIARIES) REGULATIONS, 2008

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In respect of –

Leo Global Commodities Private Limited

[Registration No. INZ000107531]

In the matter of National Spot Exchange Limited

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**BACKGROUND**

1. Securities and Exchange Board of India (hereinafter be referred to as “**SEBI**”) initiated enquiry proceedings against Leo Global Commodities Private Limited (hereinafter be referred to as “**Noticee**” / “**Leo Global**”), registered with SEBI as a commodity derivatives broker under the SEBI (Stock Brokers) Regulations, 1992 (hereinafter be referred to as “**Stock Broker Regulations**”), for the alleged violations of Regulations 5(e), 9(b) and 9(f) read with Clause A(1), A(2) and A(5) of Schedule II of the Stock Broker Regulations read with Schedule II of the SEBI (Intermediaries) Regulations, 2008 (hereinafter be referred to as “**Intermediaries Regulations**”).
2. The Noticee was a Trading and Clearing Member of the National Spot Exchange Limited (hereinafter be referred to as “**NSEL**”), which was incorporated in May, 2005 as a spot exchange for trading in commodities. NSEL organised trading in commodities after it was granted exemption from certain provisions of Forward Contracts (Regulation) Act, 1952 (hereinafter be referred to as, “**FCRA**”) by the Department of Consumer Affairs of the Ministry of Consumer Affairs, Food and Public Distribution, Government of India, vide Gazette Notification No. SO 906(E) dated June 05, 2007 (hereinafter referred to as “**2007 Exemption Notification**”), in exercise of powers conferred under Section 27 of FCRA subject to certain conditions which, *inter alia*, included “*no short sale by members of the exchange shall be allowed; that all outstanding positions of the trade at the end of the day shall result*”

*in delivery and 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”.*

3. In September 2009, NSEL allegedly introduced the concept of '*paired contracts*', i.e. buying and selling the same commodity through two different contracts at two different prices on its platform wherein investors could buy a short duration settlement contract and sell a long duration settlement contract and vice versa at the same time. It entailed occurrence of Buy Trades (T+2 / T+3) and Sell Trades (T+25 / T+36) on the same day at different prices on the platform of NSEL.
4. On February 06, 2012, the erstwhile Forward Markets Commission (hereinafter referred to as “**FMC**”) was appointed by the Department of Consumer Affairs, Government of India as the ‘designated agency’, authorizing it to collect the trade data from NSEL and to examine the same for taking appropriate measure, if needed, to protect investors’ interest. The FMC had accordingly, *inter alia*, called for the trade data from NSEL in the prescribed reporting formats. After analysing the trade data received from the NSEL, the FMC passed Order No. 4/5/2013-MKT-1/B dated December 17, 2013 in the matter (hereinafter referred to as “**FMC Order**”) wherein it was, *inter alia*, observed that 55 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*’ was being not complied with by NSEL and its members. FMC further observed that the ‘*paired contracts*’ offered for trading in the NSEL platform were in violation of the provisions of the FCRA and also in violation of the conditions specified by the Government of India in its 2007 Exemption Notification.
5. On perusal of the FMC Order, I note that the FMC had, *inter alia*, observed that the following conditions stipulated in the 2007 Exemption Notification were violated by NSEL:

- 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 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 under the aforesaid Notification.

6. Hence, it was alleged that NSEL organised trading in ‘*paired contracts*’ in violation of the 2007 Exemption Notification. It was also alleged that the Trading Members and Clearing members of the NSEL facilitated and/or participated in trading in such paired contracts which were in alleged violation of the 2007 Exemption Notification. Thus, by participating in / facilitating trading in paired contracts, such entities, allegedly, had acted in a manner detrimental to the interest of the securities market.
7. As per the information available with SEBI, the Noticee, being a Trading Member/ Clearing member of the NSEL, participated in / facilitated trading in paired contracts on the platform of NSEL in alleged violation of the provisions of Regulation 9(b) and 9(f) read with Clauses A(1), A(2) and A(5) of Schedule II of the Stock Broker Regulations. Based on this information, SEBI was *prima facie* satisfied that there were sufficient grounds to enquire into whether the Noticee, is a ‘*fit and proper person*’ to continue to hold certificate of registration as Trading and Clearing Member in terms of Regulation 5(e) of the Stock Broker Regulations read with Regulation 27(iv) of the Stock Broker Regulations read with Schedule II of the Intermediaries Regulations.

**ENQUIRY BY DESIGNATED AUTHORITY**

8. A Designated Authority (hereinafter referred to as “**DA**”) was appointed by SEBI vide order dated September 21, 2018 to conduct an enquiry against the Noticee and submit a report and make recommendation/s in terms of Regulation 27 of the Intermediaries Regulations (as applicable at the relevant time) in respect of the violations alleged to have been committed by the Noticee mentioned at para 7 above.
9. After conducting the enquiry as envisaged under Regulation 25 of the Intermediaries Regulations, the DA submitted an Enquiry Report dated December 17, 2020 (hereinafter referred to as the “**Enquiry Report**”) which, *inter alia*, observed and recommended as under:

*“In view of the facts and circumstances of the case and material placed before me, I am of the view that the Noticee is not a fit and proper person in terms of Regulation 5(e) read with Regulation 27(iv) of the Stock Broker Regulations read with Schedule II of the Intermediaries Regulations. Therefore, in terms of Regulation 27 of the Intermediaries Regulations, I recommend that the registration of the Noticee, i.e. Leo Global Commodities Pvt. Ltd. [Registration No. INZ000107531] as a commodities derivatives broker may be cancelled.”*

## **POST ENQUIRY PROCEEDINGS**

### **Show Cause Notice, Reply and Personal Hearing**

10. After considering the Enquiry Report, a post-enquiry Show Cause Notice dated January 15, 2021 ( hereinafter referred to as the “**SCN**”) was issued to the Noticee under Regulation 28(1) of the Intermediaries Regulations (as applicable at the relevant time) enclosing therewith (a) copy of the Enquiry Report, (b) copy of the letter dated December 30, 2014 of the Department of Economic Affairs (DEA) Ministry of Finance and (c) a copy of the order dated August 22, 2014 passed by the Hon’ble Bombay High Court in Criminal Bail Application No. 1263 of 2014 in the case of *Jignesh Prakash Shah Vs. The State of Maharashtra*. The SCN was issued to the Noticee calling upon it, as to why action as recommended by the DA including any other action as deemed fit should not be taken against the Noticee, by the Competent Authority. The Noticee, vide letter dated March 01, 2021, filed its reply and made the following submissions:

- (i) The reply of the Noticee may be read in conjunction with the Noticee's earlier reply given vide letter dated October 29, 2018.
- (ii) The Noticee denies all the allegation raised in the SCN;
- (iii) The Noticee was trading in the commodities contracts including alleged paired contracts on behalf of its clients.
- (iv) NSEL was functioning in complete public knowledge and was permitted to provide the trading platform for paired contracts and hence there was no reason for the Noticee to question the legality of such product launched by NSEL. During the relevant time when the members of NSEL were trading in commodities contracts, including alleged paired contracts they were governed by NSEL Bye laws and its Business Rules and Circulars. The

Noticee had no say in the matter of designing the commodities contracts including alleged paired contracts as it was entirely within the domain of NSEL. The concept of paired contract was designed /introduced and operationalized by NSEL and the Noticee as a broker of NSEL provided the product to the clients as received from NSEL. It is incorrect to suggest or infer that because the Noticee traded in paired contracts, it was closely associated with the NSEL and paired contracts.

- (v) The commodities brokers came under the umbrella of SEBI Regulations only after September 28, 2015 and hence they cannot be made liable for violation of SEBI Regulations for their acts or omissions prior to September 28, 2015.
- (vi) In view of the provisions in Section 29A (2)(e) of the FCRA, SEBI could only initiate prosecution proceedings against the members of the NSEL for alleged violation of FCRA and cannot initiate the enquiry proceedings under the Intermediaries Regulations, which are attracted when an intermediary allegedly violates any of the conditions of the Certificate of Registration or any of the provisions of the Securities laws and the regulations framed thereunder. The present proceedings under the Intermediaries Regulations do not fall within the purview of aforesaid section 29A(2)(e).
- (vii) There are no specific allegations against the Noticee and that no charges in particular has been levied by the DA, wherein, no specific documentary evidence has been recorded by the DA in its Report. Therefore, the Show cause notices ought not have been issued against the Noticee in view of the DA Report.
- (viii) The Noticee, as a commodity broker, in the normal course was not required to assess the legality of the product introduced by the exchange. It was the responsibility of the Regulator/ Government of India ("GOI") to ensure that an exchange is operating within the parameters of law. In the instant case, the Regulator as well as GOI failed to take any preventive action for more than three (3) years when NSEL was permitting trading of alleged paired contracts on its platform.
- (ix) NSEL had always projected the alleged paired contracts as legal and permissible contracts within the ambit of the gazette notification dated June

5, 2007 granting it exemption from the compliance of the provisions of FCRA.

- (x) The SCN issued by DA does not specify any of the rules, regulations and bye laws of NSEL which have been allegedly violated by the Noticee. It is in fact pertinent to note that the regulation 9(b) refers to the rules, regulations and bye laws of the stock exchange. NSEL is not a stock exchange within the meaning of Stock Broker Regulations. The application of regulation 9(b) therefore in the instant case is misconceived and legally untenable.
- (xi) SCN issued by DA was not accompanied with the relevant information, data, trade/order log, investigation report or any other material relied upon by SEBI for issuing the SCN;
- (xii) The SCN doesn't provide a copy of the observations of the Central Government (relied upon in the "communication of Order appointing the Designated Authority) that NSEL has violated exemption conditions permitting it to allow trades in one-day forward contracts;
- (xiii) The Noticee was served with an email dated July 20, 2020 forwarding an excel sheet of purported certain trade data from Economic Offence Wing, Mumbai and SEBI sought the Noticee's response to the same. The purported data pertaining to the alleged trades in paired contract on NSEL are non-verified and the Noticee sought inspection of the records of SEBI based on which the data has been extracted. Since the SCN issued by the DA is not based on any investigation or inspection undertaken by SEBI, the same is legally untenable. Any reliance upon the said documents would be against the principles of natural justice and the same would vitiate whole proceedings against the Noticee. In terms of regulation 17(1) & (2)(c) of Intermediaries Regulations, it is essential for SEBI to undertake inspection of the books, accounts, records and documents of an intermediary to ascertain whether any circumstances exist which would render the intermediary unfit or ineligible.
- (xiv) The enquiry report has been prepared based on wrong assumption that the Noticee has been provided with the documents relied upon by SEBI while the fact is that no such documents whatsoever were ever provided to the Noticee and consequently principles of natural justice had not been adhered to while conducting the enquiry proceedings. The documents which were

available in public domain were provided to the Noticee, however, case specific documents have not been provided to the Noticee till date.

- (xv) The letter dated November 20, 2015 of the Ministry of Finance (issued after Notification of the Repeal of FCRA and vesting of jurisdiction in SEBI in respect of commodities markets) has direct bearing on the question of jurisdiction of SEBI on spot market. The said letter of Ministry of Finance (MOF) clearly states that SEBI is not expected to deal with matters which were not dealt with by the erstwhile FMC.
- (xvi) No such documents viz FMC Order dated December 17, 2013, Hon'ble Bombay High Court Judgment in 63 Moons' Technologies, Interim Report of EOW etc. were ever provided to the Noticee and hence DA's reliance thereon without providing copies thereof to the Noticee, is patently wrong and violative of the principles of natural justice. The Noticee was provided a copy of the letter dated December 30, 2014 of DEA, Ministry of Finance and Order dated August 22, 2014 passed by Hon'ble High Court of Bombay, recently vide SEBI's current Show Cause Notice dated January 15, 2021. However, copy of the order dated April 30, 2019 has not been provided to the Noticee. The Letter dated December 30, 2014 pertains to Ministry of Finance's observations regarding NSEL and there is nothing specific against this Noticee. FMC order dated December 17, 2013 has found fault with the operations of NSEL for launching paired contracts and the role of its promoters and key managerial personnel. Neither the Noticee was a party to the said proceedings nor the Court had considered the role/ activities of the Noticee as a member of NSEL. Hence, the said order has no relevance so far as the Noticee is concerned.
- (xvii) The Noticee had traded / facilitated trading in the paired contracts as a member of NSEL in accordance with the business rules and regulations of NSEL. As regards Rs.16,54,39,530 as alleged in the EOW Report, the said amount is due and receivable to our clients for trades and contracts executed on their behalf from NSEL. The EOW Report doesn't hold the Noticee responsible for indulging in any of the activities as per objective of EOW investigation. Further, the Show Cause Notice dated September 25, 2018 and also the enquiry report has neither alleged nor brought out any of the said activities of the Noticee in particular.

- (xviii) NSEL was incorporated in the year 2005 and had launched these alleged paired contracts somewhere in the year 2007. The Noticee became member of NSEL in November, 2008. However, by this time the said paired contract product was widely traded in the market and became very popular amongst the risk savvy investors having investible surplus and intending to invest it in the relatively low risk with reasonable return products. In this background, few of the Noticee's clients were constantly requesting it to allow them to invest their funds in this product as the Noticee already has necessary infrastructure in place but was not active in that product. After carrying out due diligence of product on the basis of inquiries with NSEL officials, fellow brokers and their clients who were already participating in this product since last few years, the Noticee initially started trading activity in proprietary account to test the product and in the absence of any specific adverse reasons, the Noticee had allowed some clients to trade in this product who approached the Noticee for that on their own instance.
- (xix) The Noticee executed trades only for few clients who had approached it at their own instance. The Noticee neither marketed this product nor it had intention to do so. The total turnover of the Noticee for the financial years 2011-2014 to the tune of ₹258.44 crores, out of which the Noticee earned brokerage of ₹23,26,582.91. There has been no complaints or grievances or allegations of any violations of regulations against the Noticee.
- (xx) That upon slightest hints about possible violations of any regulatory framework appearing in the public domain through media reporting, the Noticee had promptly taken cognizance of the potential risk, educated and persuaded its clients to exit from the product.
- (xxi) As per the Show Cause Notice dated January 15, 2021 the Noticee being a member of NSEL had allegedly participated and/or facilitated trading into paired contracts on the platform of NSEL during the period of September 2009 to August 2013 which was in alleged violation of notification dated June 5, 2007 as well as Regulation 9(b) and 9(f) r/w Clause A(1), A(2) and A(5) of Schedule II of the Broker Regulations. The Ld. DA has not found the Noticee guilty of the alleged violation of Regulation 9(b) and 9(f) r/w Clause A(1), A(2) and A(5) of Schedule II of the Broker Regulations. In the absence of any finality of guilt on the violation of aforementioned provisions of Broker



Regulations, the Ld. DA has jumped to the conclusion that by trading in paired contracts at NSEL the Noticee can be viewed as having close association with NSEL and consequently not a fit and proper person. The Ld. DA has recommended cancellation of the certificate of registration of the Noticee as a Commodity Derivatives Broker, which is not tenable in law.

(xxii) a broker operating on the stock exchange cannot be treated as a close associate of a stock exchange, unless there is a common ownership, management or control.

(xxiii) The commodities contracts including alleged paired contracts were introduced by the Board/ Management of NSEL with the prior concurrence of the Forward Market Commission ("FMC"). The Noticee as a member of NSEL had no other option but to trade in such contracts by observing the business rules and regulations of NSEL. There is no allegation whatsoever that the Noticee has committed any breach of the business rules and regulations of NSEL as applicable to the trading in paired contracts. Hence it is very unfair to blame the members of NSEL for the product which was introduced by NSEL with the concurrence of FMC.

11. While the extant proceedings in the present matter were ongoing, 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 the NSEL matter. Aggrieved by the said SEBI orders, the entities filed separate appeals before the Hon'ble Securities Appellate Tribunal (hereinafter referred to as "**Hon'ble SAT**"). The Hon'ble SAT, vide common order dated June 9, 2022, remanded the aforesaid orders to SEBI to decide these matters afresh within six months from the date of the said SAT 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.....”*

12. Subsequently, in August 2022, the present matter was allocated to me. In the light of the aforesaid SAT Order and certain other orders passed by the Hon'ble SAT in similar set of cases, it was felt necessary to furnish certain additional documents/material to the Noticee before concluding the present proceedings. Accordingly, a supplementary show cause notice (hereinafter referred to as “**SSCN**”) dated October 12, 2022 enclosing therewith a copy of the SEBI Complaint dated September 24, 2018 filed with EoW, Mumbai, a copy of the FIR dated September 28, 2018 and a copy of the amended Schedule II of the Intermediaries Regulations was issued to the Noticee and the Noticee was granted 15 days' time to file its reply, if any from the date of receipt of the said SSCN. I note from the material available on record that the Noticee, vide letter dated December 01, 2022, filed its reply to the SSCN and made the following submissions:
- i. The reply of the Noticee may be read in conjunction with the Noticee's earlier reply given vide letter dated March 01, 2021.
  - ii. The Noticee denied contents of the supplementary show cause notice.
  - iii. The law of limitations has been clearly given a go-by in the instant case, wherein SEBI has issued the said Show Cause Notices after a lapse of more than 5 years from the cause of action, which has been allegedly relied upon/ referred to in the said Show Cause Notices.
  - iv. Pursuant to the power granted under Section 29A of FCRA, 1952, SEBI, vide its complaint letter dated September 24, 2018 (just before the expiry of the limitation period of 3 years) lodged a complaint with the EOW for appropriate action against the NSEL trading members and other members of NSEL who have traded in the alleged illegal forward contracts at NSEL in violation of provisions of FCRA. The said complaint was immediately followed by an FIR dated September 28, 2018 against 300 persons including the Noticee in the said complaint filed with EOW. The present complaint has been filed by SEBI on September 24, 2018 at the 11<sup>th</sup> hour without following any of the rules and regulations as laid down by the law, just to ensure the limitation is not ousted.

- v. The intermediaries were merely the facilitators of the transaction. The role of checking the stock at the warehouse was limited to NSEL, and accordingly, warehouse charges were imposed by NSEL and borne by the Noticee. The Noticee has taken all due diligence while acting as an intermediary on behalf of its client, for which, no complaint against the Noticee has been filed by its clients.
- vi. The Noticee herein has been issued a Certificate of Registration dated November 13, 2017 by SEBI in exercise of its powers conferred by subsection (1) of section 12 of the Securities and Exchange Board of India Act, 1992.
- vii. A First Information Report (FIR) is only the first instance of reporting of a complaint that is lodged with the police. This is a preliminary document based on the one-sided statement(s) of the complainant without any adjudication of the same. Such an FIR is far from being equivalent to a final determination. Any such adverse reliance on the FIR would be a gross violation of law and can cause grave prejudice to the Noticee in the event the ultimate decision is proved to be otherwise. Therefore, no reliance can be placed on any FIR, particularly an FIR which has been filed by SEBI itself.
- viii. It is pertinent to note that the amendment of the criteria for fit and proper person laid out in Schedule II of the Intermediaries Regulations took effect from November 17, 2021 which is much after the initiation of the present proceedings. Therefore, any retrospective reliance on such an amendment that took place later in time would be gross violation of law and principles of natural justice.
- ix. The Hon'ble Bombay High Court in its Order dated 4.12.2017 in Writ Petition No. 2743 of 2014, expressly held that brokers cannot be blamed for trading in paired contracts.
- x. Noticee had taken necessary due diligence and clients were notified of the risks of trading through the Noticee in NSEL.
- xi. There are no specific charges made against the Noticee in the interim report. The EOW Report nowhere held that the Noticee is responsible for indulging in any of the activities.
- xii. The Ld. DA failed to provide an opportunity to the Noticee under Regulation 25 of the Intermediaries Regulation, 2008, wherein it is clearly stated that the Noticee should have been given an opportunity to be heard during the alleged

enquiry. The very absence of opportunity afforded to the Noticee herein goes against the basic principles of natural justice and therefore, the said enquiry by the DA stands vitiated due to the non-adherence to the principles of Natural Justice.

- xiii. FMC order dated December 17, 2013 has found fault with the operations of NSEL for launching paired contracts and the role of its promoters and key managerial personnel and there has been no whisper against the Noticee.

13. In compliance with the principles of natural justice, an opportunity of personal hearing was granted to the Noticee before me on December 14, 2022 through video conferencing and the Noticee vide its email dated December 01, 2022 confirmed its presence for the said hearing.
14. On the date of hearing, the Noticee was represented by Mr. Uttam Singhal and Mr. Ramakant Singhal, Directors of the Noticee alongwith Mr. Som Raj Choudhury, Advocate who reiterated the submissions made by the Noticee vide its letters dated October 29, 2018, March 01, 2021 and December 01, 2022. The Authorized Representatives admitted that, they had executed trades on the NSEL platform starting from March 19, 2012 to July 26, 2013. Further, as requested, one week's time was granted to the Noticee to make additional submissions, if any. Accordingly, vide letter dated December 21, 2022, the Noticee, made additional submissions in the matter which are summarized as under:
- (i) Leo Global was incorporated on August 17, 2000. The company is a member of the MCX and NCDEX. The company has a diverse clientele; this includes small-to-large size corporates in agri-business, metals, foods and bullion trade, as well as individuals.
  - (ii) Leo Global applied for membership on NSEL in the year 2008 and had received approval for trading on July 29, 2008 and the clearing member ID only on February 05, 2010. The company started trading with NSEL for the first time in the year 2012. The first transaction was in pro account (for Leo Global from its own account) on March 19, 2012 with an attempt to understand the process of the transaction under the NSEL. The said transaction was done purely in good faith to understand the system and its functioning in the said platform.
  - (iii) After being satisfied and understanding the process of transaction, Leo Global started trading in the commodities contracts including alleged paired contracts

on behalf of its Clients. During the entire transaction period from March 19, 2012 to July 26, 2013, Leo Global had only 10 clients (including Leo Global itself). Leo Global had very limited transactions on NSEL platform.

- (iv) The Noticee had started trading on behalf of its clients on the said platform in 2011-12 and transactions were conducted smoothly. The last transaction made by Leo Global on the platform of NSEL was on 26.07.2013. Total turnover for the period FYs 2011-2014 for transactions on the NSEL was to the tune ₹258.44 Crores out of which the brokerage received by Leo Global for the said period was of ₹23.26 Lakhs only.
- (v) Leo Global has neither been involved in propagating the concept of NSEL nor advertised/ marketed for it.
- (vi) Leo Global was granted a Certificate of Registration dated November 13, 2017 by SEBI. The certificate conferring the Noticee to be fit and proper was issued in 2017 and the alleged accusations on the Noticee are dated for the transactions made by the Noticee in the year 2012 and 2013. That, had there been a question of Leo Global not being 'fit and proper' person, the said certificate could not have been issued by the SEBI.

## **CONSIDERATION OF ISSUES AND FINDINGS**

15. I have carefully perused the post enquiry SCN, SSCN along with all the documents attached therewith, the replies submitted by the Noticee, the oral submissions made by the Noticee during the course of the personal hearing along with all the other material/ information available on record. After considering the allegations made/ charges levelled against the Noticee in the instant case, I note that the only issue that arises for 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.
16. Before considering the issue on its merits, I note that the SCN dated January 15, 2021 called upon the Noticee to show cause as to why action as recommended by the DA, including passing of appropriate direction should not be taken against the Noticee in terms of regulation 28 of the Intermediaries Regulations. I note that by the amendments made to Intermediaries Regulations on January 21, 2021, regulation 27 which dealt with recommendations for actions which could be made by DA in case of default, has been substituted and regulation 28, which dealt with procedure for action

on receipt of the recommendation from DA, has been omitted and these matters now stand governed by the Regulations 26 and 27, respectively. In the present case, I note that prior to the aforesaid amendment, procedure for conduct of enquiry proceedings before DA and Competent Authority (CA) was provided under regulations 25 to 28 of the Intermediaries Regulations wherein regulation 25 dealt with issue of SCN by the DA, regulation 26 dealt with reply of SCN by the Noticee, regulation 27 dealt with recommendation for actions which could be made by the DA and regulation 28 dealt with conduct of proceedings before the CA, like issue of SCN, hearing and passing of final order. After the aforesaid amendment, regulation 25, as substituted, deals with holding of enquiry proceedings before DA, regulation 26 deals with recommendation for actions which can be made by the DA and regulation 27 deals with conduct of enquiry proceedings before the CA and passing of order by the CA. Thus, the proceedings before CA which were earlier governed by the provisions of regulation 28 are now governed by the provisions of regulation 27 with certain modifications. Therefore, the new regulation 27 is regarded having force continuously (by virtue of pre-existing regulation 28) and the modification or changes are treated as amendment coming into force with effect from the date of enforcement of new regulation 27 i.e. January 21, 2021. Accordingly, I note that the present proceedings can be concluded under the amended provisions of the Intermediaries Regulations and for the violations committed by the Noticee, directions under regulation 27 of the Intermediaries Regulations can be issued.

17. The Noticee has also submitted that the DA has failed to provide an opportunity for personal hearing to the Noticee under Regulation 25 of the Intermediaries Regulation, 2008, wherein it is clearly stated that the Noticee should have been given an opportunity to be heard during the alleged enquiry. The very absence of opportunity of being heard extended to the Noticee herein goes against the basic principles of Natural Justice and therefore, the said enquiry by the DA stands vitiated due to the non-adherence to the principles of Natural Justice. In this regard I note that, the Intermediaries Regulations were amended with effect from January 21, 2021, wherein Regulation 25 was replaced. As per Regulation 25 (6) of the amended regulations, the DA shall grant an opportunity of personal hearing to the Noticee. However, no such requirement was mandated under the pre-amended regulations. I also note that the proceedings in the present matter before the DA have been completed before the said amendment to the Intermediaries Regulations mandating

the DA to grant personal hearing came into being and the DA has submitted the report between the said amendment to the Intermediaries Regulations came into being. In view of that, I do not find any merit in the argument of the Noticee that the enquiry by the DA stands vitiated due to the non-adherence to the principles of Natural Justice and therefore reject the said contention.

18. Prior to moving forward with considering the said issue as stated at para 15 above, it is pertinent to refer to the common order dated June 09, 2022<sup>1</sup> passed by the Hon'ble SAT which is also referred in the preceding paragraph 11. The Hon'ble SAT, while setting aside and remanding the earlier WTM Orders passed during February 2019, had made the following observations (relevant to the present case as well):

- (a) Observations of the Bombay High Court in the matter of *63 Moons vs. Union of India*<sup>2</sup> cannot be relied upon as the said judgement has been set aside in appeal<sup>3</sup> by the Hon'ble Supreme Court vide judgment dated April 30, 2019.
- (b) Observation from the Order dismissing the Writ Petition filed by NSEL against the invocation of the Maharashtra Protection of Interest of Depositors (in Financial Establishments) Act, 1999 ("MPID Act") (*NSEL vs. State of Maharashtra*<sup>4</sup>) cannot be relied upon, as in a subsequent Writ Petition<sup>5</sup> moved by 63 Moons, a Division Bench of the Hon'ble Bombay High Court has held that NSEL is not a financial establishment and therefore, the provisions of the MPID Act are not applicable. The prima facie observations cannot be the basis to judge the reputation, character or integrity of NSEL.
- (c) Observations in the bail rejection order dated August 22, 2014, passed by the Hon'ble Bombay High Court in the matter of ***Jignesh Prakash Shah vs. The State of Maharashtra***, cannot also be relied upon as the observations made in a bail order were limited to the fact as to whether the bail should be granted or not.
- (d) Reliance placed on decisions of the Hon'ble Tribunal in the matter of ***Jermyn Capital vs. SEBI***<sup>6</sup> and ***Mukesh Babu Securities vs. SEBI***<sup>7</sup> is misplaced, as decisions in the said matters are distinguishable on facts. Jermyn Capital was held

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<sup>1</sup> Appeal No. 214 of 2019 Geofin Comtrade Ltd Vs. SEBI, Appeal No. 217 of 2019 Philip Commodities India Pvt. Ltd Vs. SEBI, Appeal No. 218 of 2019 IIFL Commodities Ltd Vs. SEBI, Appeal No. 288 of 2019 Anand Rathi Commodities Ltd Vs. SEBI and Appeal No. 288 of 2019 Anand Rathi Commodities Ltd Vs. SEBI

<sup>2</sup> Writ Petition No. 2743 of 2014

<sup>3</sup> Civil Appeal No. 4467 of 2019

<sup>4</sup> Writ Petition No. 1403 of 2015

<sup>5</sup> Writ Petition No. 1181 of 2018

<sup>6</sup> Appeal No. 26 of 2006 decided on September 06, 2006

<sup>7</sup> Appeal No. 53 of 2007 decided on December 10, 2007

to be in relation to an Interim Order passed by SEBI, and the Tribunal was of the view that the criteria for passing an Ad Interim Order are based on a different criterion, namely prima facie case, the balance of convenience and irreparable injury which are distinct and different while considering an application for grant of Certificate of Registration. The decision in the matter of *Mukesh Babu Securities* was of a criminal complaint filed against the Chairman of the Company. The Tribunal noted that there is no evidence to show that any proceedings have yet been initiated against the appellants in the matter under consideration.

- (e) Reputation of the applicant cannot be lightly considered based on observations which are not directly related to the applicant.
- (f) SEBI Order does not state for how long the rejection of application will continue. The Hon'ble Tribunal was of the view that the rejection cannot continue indefinitely, and in such cases, a time period should be provided during which the applicant will become ineligible to seek fresh registration.
- (g) Grant Thornton Forensic report commissioned by SEBI does not find any close connection between the applicant and the NSEL. This is overlooked by SEBI.
- (h) With respect to the additional material available, the Hon'ble SAT observed that, "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. It will also be open to SEBI if it considers necessary, to conduct an independent enquiry proceeding against the connected entities and persons associated with the brokers against whom evidence is available."

19. As noted above, taking cognizance of the order passed by the Hon'ble SAT on June 09, 2022 (referred supra), a SSCN dated October 12, 2022 was issued to the Noticee calling upon the Noticee to show cause as to why the following information/material along with the Enquiry Report dated December 17, 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 Economic Offence Wing ('EOW');



- b) First Information Report ('FIR') dated September 28, 2018; and
  - c) Schedule II of the Intermediaries Regulations (Amended with effect from November 17, 2021).
20. Before considering the matter on merits and test the compliance of the Noticee with the '*fit and proper person*' criteria, on the basis of the material that has been brought on record, it would be appropriate to look at the background and understand the nature of the '*paired contracts*' that were offered on the NSEL – which ultimately is the cause / genesis of the current proceedings. While undertaking this exercise, I will not be independently recording any findings on the nature of the contracts that were entered on the NSEL platform or commenting on the actions of any entity which is not a party to the present proceedings. I will, however, be relying on the observations made by other authorities including the Hon'ble Supreme Court in the matters of **63 Moons Technologies Ltd. vs. UOI**<sup>8</sup> (hereinafter referred to as the "**merger petition**") and **The State of Maharashtra Vs. 63 Moons Technologies Ltd**<sup>9</sup> (hereinafter referred to as the "**MPID Matter**"), wherever appropriate.

#### **Transactions in the nature of 'paired contracts' on NSEL:**

21. 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. NSEL was incorporated in 2005 as an electronic exchange for spot trading of commodities. On June 5, 2007, the Ministry of Consumer Affairs ("MCA"), Government of India, issued a Notification SO 906(E) under Section 27 of the FCRA granting conditional exemption from the provisions of that Act with respect to (i) forward contracts, (ii) for sale and purchase of commodities, of one-day duration traded on NSEL. The conditions, *inter alia*, placed an absolute bar on short sales and stipulated that all outstanding positions at the end of the day must 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. Thereafter, NSEL commenced operations in October 2008.
22. As noted from the FMC order, NSEL introduced, on its platform, the concept of '*paired contracts*', in September 2009, which involved buying and selling the same commodity through two different contracts at two different prices wherein investors

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<sup>8</sup> Civil Appeal no. 4476 of 2019

<sup>9</sup> Civil Appeal No. 2748-49 of 2022

could buy a short duration settlement contract and sell a long duration settlement contract or vice versa, with the same counterparty at the same time. In other words, the 'paired contract' involved two simultaneous transactions being undertaken at the same time with the same counterparty—one being a purchase transaction (settling at T+2 or T+3) and the other being a sale transaction (settling at T+25 or T+36), at different prices on the platform of NSEL. The transactions were structured in such a manner that buyer of the short duration contract always ended up making profits.

23. As mentioned at para 4 above, FMC, after analysing the trade data as received from NSEL, vide order No. 4/5/2013-MKT/B dated December 17, 2013 ("FMC Order") observed that: "55 contracts offered for trade on NSEL were with settlement period exceeding 11 days and all such contracts traded on NSEL were in violation of provisions of FCRA" and "the condition of 'no short sale by members of the exchange shall be allowed' was not being met by NSEL".
24. Further, in the above mentioned Order, FMC, *inter alia*, held that the contracts traded on NSEL have violated certain conditions stipulated in the 2007 Exemption Notification, which granted permission to NSEL to offer spot trading in commodities which, *inter alia*, included *"no short sale by members of the exchange shall be allowed; that all outstanding positions of the trade at the end of the day shall result in delivery"* and 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"*.
25. It is clear from the order of FMC 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 2007 Exemption Notification. I note from the FMC Order<sup>10</sup> that the 55 contracts offered for trade on NSEL were with settlement periods exceeding 11 days and all such contracts traded on NSEL were in violation of the provisions of FCRA. I further 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 as contained in FCRA, I note that FMC was of the view that all the contracts traded on NSEL which provided settlement schedule exceeding 11 days were treated as Non-Transferable Specific Delivery contracts.

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<sup>10</sup> Order No. 4/5/2013-MKT-1/B dated December 17, 2013

26. Therefore, it is noted that even though it was stipulated in the 2007 Exemption Notification that, only contracts of one-day duration were permitted to be offered on NSEL, FMC, in its Order, relying on the definition of “*forward contract*” under FCRA held that, NSEL was allowed to trade only in one-day forward contracts and was obliged to ensure delivery and settlement within 11 days. I note the observation in the FMC order that NSEL had permitted 55 contracts of various commodities having duration longer than 11 days and these contracts were, *ex facie*, in contravention to the exemption granted to NSEL. It is pertinent to note that all the 55 contracts that were advertised by NSEL, and which are captured in the Hon’ble Supreme Court’s Judgement in the matter of MPID matter, were for durations exceeding 11 days.
27. I note that the Hon’ble Supreme Court in the matters of NSEL has also extensively commented on the nature of the ‘paired contracts’ traded on NSEL. The said observations made by the Hon’ble Supreme Court are as under:
- a. the Two-Judge Bench of the Hon’ble Supreme Court in the course of determining the validity of the amalgamation order in the matter of merger petition, vide judgment dated April 30, 2019, had observed as under:

*“55. 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 are distinct from the sale and purchase transactions in commodities and were, thus, in breach of both the exemptions granted to NSEL and the FCRA.” (emphasis supplied)***

- b. the Hon’ble Supreme Court in the MPID matter vide judgement dated April 22, 2022, has drawn reference to the presentations made by NSEL in respect of the ‘paired contracts’. Upon analysing the presentations made, the Hon’ble Supreme Court has observed 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." (emphasis supplied)

28. I, therefore, note that the Hon'ble Supreme Court has already commented on the nature of the 'paired contracts' offered on the NSEL platform. In the case of *63 Moons Technologies Ltd. vs. UOI*, the Hon'ble Supreme Court 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 has held that such transactions come within the definition of 'deposits' under the MPID Act.
29. It is further noted that the Hon'ble Supreme Court, in the MPID matter, had extensively referred to the claims made on the website of the NSEL and the contents of the publicity material and other investor resources. As seen from the order of the Hon'ble Supreme Court, NSEL was advertising an annualized return of about 16% p.a. for the 'paired contracts' traded on its platform. The return offered was the same across commodities. The return remained the same irrespective of the duration of the contract. For example, a T+2 & T+25 paired contract in steel had the same offered return as a T+ 2 & T + 35 paired contract in castor oil. The 'paired contracts', it is noted, were being marketed as an alternative to fixed deposits.
30. I note that the FMC Order and both the judgments of the Hon'ble Supreme Court discuss in detail that, NSEL 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. It is further noted from the judgement of the Hon'ble Supreme Court in the MPID matter that the overwhelming majority of the sale leg of the 'paired contracts' which were executed were naked short sales i.e. the

commodities to back such sales were not available at the designated warehouses of the NSEL.

31. The above referred paired contracts being in contravention of the provisions of FCRA and the 2007 Exemption Notification, the DA, by stating that the fact of participation in trades in paired contract not being disputed by the Noticee, has observed that the Noticee, by failing to disassociate itself from, and continuing to facilitate participation in the said paired contracts, failed to act with due diligence.

**Preliminary objections raised by the Noticee:**

32. The Noticee has submitted that the present proceedings have been initiated in haste just before the expiry of the limitation period against the Noticee as the proceedings under FCRA could have been initiated by SEBI within 3 years from the date on which the FCRA is repealed and the Noticee was issued the notice for the present proceedings barely few days before the completion of 3 years. Further the Noticee has contended that the law of limitation has been clearly given a go-by as the Show Cause Notice was issued by the DA after a lapse of more than 05 years from the cause of action.
33. In this regard, I note that the statutory timeline prescribed by the FCRA under Section 29A(2)(e) of the FCRA empowered SEBI to initiate fresh proceedings within a period of 3 years from the cessation of the FCRA. The relevant extract of FCRA is produced hereunder—

*“(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;”*

In this regard, I note that FMC has merged with SEBI on September 28, 2015 and SEBI has filed a complaint dated September 24, 2015 with the EoW, Mumbai, *inter alia*, against the Noticee and the same is made within the time limit specified under the aforesaid provision. In view of the same, I am of the view that SEBI is within its regulatory/ statutory powers to initiate appropriate proceedings against the Noticee within a period of 3 years and the same was done within the prescribed time limit. Therefore, I find no merit in the argument of the Noticee and I am inclined to reject the aforesaid contention of the Noticee.

34. The Noticee has further submitted that SEBI does not have the jurisdiction to deal with the Spot Market in terms of letter dated November 20, 2015 of the Ministry of Finance. Since spot markets/ ready delivery contracts were not being regulated by the FMC, SEBI is not expected to take upon itself any regulatory function with regard to such markets. Accordingly, the merger of FMC with SEBI cannot empower SEBI to regulate the Spot Market. In this regard, without going into the merits of the contention that whether SEBI has the authority to regulate Spot Market or not, 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 view that SEBI is within its jurisdiction to determine the fit and proper status of the Noticee.
35. The Noticee has further submitted that the appointment of the Designated Authority (DA) in the present matter is bad in law as the same was done by the Whole Time Member and not the Executive Director, as is required under the Intermediaries Regulations. In this regard, I note that Section 3(2) of the Securities and Exchange Board of India (Delegation of Powers) Order, 2015 specifically provides that, "*The powers and functions delegated to any member or officer of the Board or authority under the Order can be exercised by any officer or authority higher in grade or rank or position to him*". Thus, in presence of a valid delegation conferred upon by the statute, I find that the Noticee's challenge to the appointment of DA by the Whole Time Member of SEBI, who is an authority higher in grade to the Executive Director of SEBI, is devoid of any merit.
36. The Noticee has also argued that it has not been provided with all the documents which have been relied upon while issuing the notice and the same amounts to violation of the principle of natural justice. The Noticee has submitted that only those documents have been provided to the Noticee which were available in public domain and case specific documents have not been provided to the Noticee. In this regard, I note that the trade details of the Noticee were duly provided by the DA, to the Noticee, vide email dated July 20, 2020. Further, the Noticee has specifically argued that material such as the FMC order and the judgment of the Hon'ble Supreme Court in the merger petition has not been provided to the Noticee. In this regard, I note that such publicly available material has not been

relied upon in the present matter to draw any adverse inference against the Noticee and has only been relied upon to explain the nature of the paired contracts which were being traded on the NSEL platform. Thus, I note that vide email dated July 20, 2020, SCN dated January 15, 2021 and SSCN dated October 12, 2022 the Noticee has been provided with the relevant and relied upon documents, including trade data in the matter. Accordingly, I am of the view that the principles of natural justice have been duly complied with in the matter and the Noticee's contention with regard to non-supply of relevant documents in the matter is misplaced.

### **Fit and proper person criteria**

37. Now, I would be proceeding to deal with the main issue in hand in the present case which is whether the Noticee satisfies the '*fit and proper person*' criteria laid down under Schedule II of the Intermediaries Regulations. Before moving forward, it would be appropriate to take a look at the relevant provision of the SEBI Act, Broker Regulations and the Intermediaries Regulations (as they exist on date) which are reproduced as under for reference:

#### ***SEBI Act***

##### ***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.*

#### ***Broker Regulations***

##### ***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 Enquiry Proceeding Regulations.**

27. A stock broker or a sub-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 or a sub-broker, as the case may be, if he—

(i) ....

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

**SCHEDULE II**

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

**CODE OF CONDUCT FOR STOCK BROKERS**

**[Regulation 9]**

**A. General.**

(1) *Integrity:* A stock-broker, shall maintain high standards of integrity, promptitude and fairness in the conduct of all his business.

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

(3) ....

(5) *Compliance with statutory requirements:* A stock-broker shall abide by all the provisions of the Act and the rules, regulations issued by the Government, the Board and the Stock Exchange from time to time as may be applicable to him.”

**Intermediaries Regulations:**



**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 fulfill 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 proceedings 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.*

38. I note that regulation 5(e) of the Broker 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 Intermediaries Regulations, 2008 was amended vide SEBI (Intermediaries) (Third Amendment) Regulations, 2021 with effect from November 17, 2021.
39. 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 from the records that the Noticee is holding a certificate of registration No. INZ000107531 dated November 10, 2017 (the Noticee in its reply has mentioned that it was issued a certificate of registration dated November 13, 2017). 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 onetime 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.

40. In this context, as per reply of the Noticee dated December 21, 2022, I note that the Noticee had started its trading through NSEL from March 19, 2012 and its last trade was on July 26, 2013. The Noticee in the said reply has stated that "*Leo Global had limited transaction on the platform of NSEL. The said transactions were paired contracts which were legally permitted at the time of transactions.*" Further, the Noticee in its reply dated December 01, 2022 has stated "*That the Noticee started trading for itself first and thereafter, for its clients on the said platform in 2011-12 and transactions were conducted smoothly*". Further, the Noticee has also stated in its reply December 21, 2022 that it had 10 clients including itself who had conducted transactions on NSEL platform and the total trading turnover was to the tune of ₹258.44 crores and the brokerage earned by the Noticee was around ₹23.26 lakhs with respect to the 'paired contracts'. Thus, it is clear from the admissions of the Noticee that the Noticee has indulged in facilitating trading in 'paired contracts' for its clients and also traded in its proprietary account.
41. I note that the act of the Noticee in offering access to 'paired contracts' by participating in and facilitating trading in such contracts, seriously calls into question the integrity, honesty and lack of ethical behaviour on the part of the Noticee. As recorded in the FMC order and the judgements of the Hon'ble Supreme Court (mentioned supra), these contracts, were *ex facie* offered in violation of the 2007 Exemption Notification and were not spot contracts in commodities which were permitted to be traded on NSEL. The 'paired contracts'

were nothing but financing transactions masquerading as spot contracts in commodities. The execution of the trades in 'paired contracts' were not permitted under the 2007 Exemption Notification and were purely financial contracts promising assured returns under the garb of spot trading in commodities, as observed by FMC in its Order. Therefore, the Noticee by its conduct and as a member of NSEL has facilitated and/or dealt in 'paired contracts' which were in the nature of financing transaction as held by the Hon'ble Supreme Court. The Noticee, by providing access for taking exposure to 'paired contracts' has exposed its clients to the risk involved in trading in a product that did not have regulatory approval and thereby raising doubts on the competence of the Noticee to act as a registered Securities Market intermediary. Thus, I am of the view that the trading activities of the Noticee in 'paired contracts' for its clients and for itself on the NSEL platform have serious ingredients amounting to jeopardizing the reputation, belief in competence, fairness, honesty, integrity and character of the Noticee in the Securities Market.

42. I further note that Clause 3(b) of Schedule II of the amended Intermediaries Regulations lays down a list of disqualifications which includes the following:

*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;*

43. As discussed above, the Noticee has facilitated its clients to trade in 'paired contracts' and also indulged in executing proprietary trades in the 'paired contracts'. As the paired contracts were violative of the conditions stipulated in the 2007 Exemption Notification, a complaint was filed by SEBI with Economic Offences Wing, Mumbai (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 and the same are subsisting. I note that the name of the Noticee is reflected in the complaint and the FIR. I also note that the copies of the said complaint and the FIR were provided to the Noticee along with the SSCN dated October 12, 2022.

44. 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 2017, 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 lays down a list of disqualifications which includes a pending criminal complaint or information under Section 154 of CrPC filed against such an entity by the Board. It is, therefore, noted that the Noticee attracts the disqualification provided in Clause 3(b)(i) of the Schedule II of the Intermediaries Regulations.

45. Therefore, looking holistically, I find that the conduct of the Noticee is detrimental to the Securities Market, being not in conformity with the applicable code of conduct. I, therefore, note that there were enough red flags for a reasonable person to come to conclude that what was being offered as '*paired contracts*' on NSEL were not spot contracts in commodities. Given the above, I am constrained to conclude that the Noticee provided a platform for its clients to access a product and also indulged in proprietary trading in the said product, which was not permitted to trade raised serious questions on the ability of the Noticee to conduct proper and effective due diligence regarding the product itself. By failing to disassociate itself from, and continuing to facilitate participation in the said paired contracts, the Noticee failed to act with due diligence.
46. Furthermore, as mentioned in paragraph 44 above, the Noticee has also earned disqualification under Clause 3(b)(i) of the amended Schedule II of the Intermediaries Regulations on account of the complaint filed by SEBI and the FIR registered against the Noticee. In this regard it is pertinent to note that the said FIR is subsisting and has not been challenged, quashed or stayed by any competent court qua the Noticee. In this context, as observed above, I note that being a '*fit and proper person*' is a continuing 'eligibility criteria' 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 hold the field which are binding upon me, and arguments, if any, to the contrary are not maintainable.

47. The Noticee has also submitted that it was under an expectation that the products launched by the Exchange are legal and hence there was no reason for the Noticee to question the legality of such product launched 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 2007 Exemption Notification and ignorance of the conditions of the said 2007 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. Therefore, giving go-by to the terms of the 2007 Exemption Notification and attempting to camouflage the nature of the transactions brings into question of appropriateness and suitability of the continuance of the registration of the Noticee as a broker. Clearly, the actions of the Noticee has been detrimental to the interest of the Securities Market and accordingly the Noticee can no longer be called 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 Broker Regulations read with the provisions of Schedule II of the Intermediaries Regulations.
48. 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.

49. I am also aware that SEBI has passed certain orders<sup>11</sup> in the related NSEL matters where the Noticees therein have been debarred from making a fresh application seeking registration for a specified period from the date of the said order or till acquittal of the said Noticee by Courts pursuant to the charge sheet and FIR filed by/with EOW, whichever is earlier. I find that present matter at hand is different from that of those cases, as in the extant matter the Noticee is already holding a Certificate of Registration whereas in those cases, the entities had filed applications seeking certificate of registration. As already noted above at paragraph 44, '*fit and proper person*' criteria is a continuing requirement under the Intermediaries Regulations which the Noticee ought to comply with at all times so long it desires to remain associated with the Securities Market as a registered intermediary. Further, I note that the Hon'ble SAT in its order dated June 09, 2022 (pertaining to entities whose application for registration was rejected) has observed that the period for which the noticees cannot apply for registration needs to be specified by SEBI. Having noted the aforesaid observation of the Hon'ble SAT, I am of the view that since the recommendation in the present matter is of cancellation and not of rejection of the application, the necessity of specifying a period of time may not arise in this order (as in the case of entities desiring to be registered as market intermediaries) as this forum cannot presume whether such entity wishes to reapply to be a market intermediary or not. If it chooses to do so, it will have to be assessed at such point of time if it is fit and proper as per the extant and applicable regulations.

50. The limited scope of the present proceedings is to see whether the indulgence, engagement and promotion of such activities could be held to be beneficial to the

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<sup>11</sup> Orders dated November 29, 2022 in respect of Motilal Oswal Commodities Brokers Pvt. Ltd. (at [https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-respect-of-motilal-oswal-commodities-broker-pvt-ltd-\\_65602.html](https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-respect-of-motilal-oswal-commodities-broker-pvt-ltd-_65602.html)), Anand Rathi Commodities Ltd. (at [https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-the-matter-of-anand-rathi-commodities-ltd-\\_65604.html](https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-the-matter-of-anand-rathi-commodities-ltd-_65604.html)), Geofin Comtrade Limited (previously known as Geojit Comtrade Limited) (at [https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-the-matter-of-geofin-comtrade-limited-previously-known-as-geojit-comtrade-limited\\_65597.html](https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-the-matter-of-geofin-comtrade-limited-previously-known-as-geojit-comtrade-limited_65597.html)), India Infoline Commodities Ltd. (at [https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-the-matter-of-india-infoline-commodities-ltd-\\_65595.html](https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-the-matter-of-india-infoline-commodities-ltd-_65595.html)) and Phillip Commodities India Pvt. Ltd. (at [https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-the-matter-of-phillip-commodities-india-pvt-ltd-\\_65593.html](https://www.sebi.gov.in/enforcement/orders/nov-2022/order-in-the-matter-of-phillip-commodities-india-pvt-ltd-_65593.html)) in the matter of NSEL.



development of Securities Market or the same contain elements that are potentially dangerous and detrimental to the interest, integrity, safety and security of the Securities Market. In this respect, the undisputed fact, as recorded in the FMC order and Orders of the Hon'ble Supreme Court (as mentioned supra), that the scheme of 'paired contracts' traded on the NSEL ultimately has caused loss to the market which itself casts serious aspersion on the conduct, integrity and reputation of, inter alia, the Noticee who participated in / or facilitated such 'paired contracts' and therefore, its continuing role in the Securities Market cannot be viewed as good and congenial for the interest of the investors or of the Securities Market.

51. Given the above discussions and deliberations, I am constrained to conclude that the act of the Noticee providing access to its clients to participate in a product and also indulging in proprietary trades in the said 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 presumably, driven by its desire to earn brokerage and / or profit. Further, as per findings recorded above, the Noticee also attracts the disqualification provided in Clause 3(b)(i) under the amended Schedule II of the Intermediaries Regulations in view of the complaint filed by SEBI and the pending FIR against the Noticee which is subsisting/pending as on date. Further, it is also not the case of the Noticee that said FIR filed 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 and hence, the continuance of the Noticee as a registered broker will be detrimental to the interest of the Securities Market. Therefore, such activities of the Noticee as a registered broker cannot be condoned and deserve appropriate measure to prevent such wrong doings recurring to the detriment of the interest of the Securities Market.

52. In view of the above, I concur with the recommendation made by the DA.

## ORDER

53. I, therefore, in exercise of powers conferred under Section 12(3) and Section 19 of the SEBI Act, 1992 read with Regulation 27 of the Intermediaries Regulations, 2008 cancel the Certificate of Registration (bearing no. INZ000107531) of the Noticee viz. Leo Global Commodities Private Limited.

54. The Noticee shall, after receipt of this order, immediately inform its existing clients, if any, about the aforesaid direction in paragraph 53 above.
55. Notwithstanding the direction at paragraph 53 above, the Noticee shall allow its existing clients, if any to withdraw or transfer their securities or funds held in its custody, within 15 days from the date of this order. In case of failure of any clients to withdraw or transfer their securities or funds within the said 15 days, the Noticee shall transfer the funds and securities of such clients to another broker registered with SEBI within a period of next 15 days thereon, under advice to the said clients.
56. This Order shall come into force with immediate effect.
57. The above Order is without prejudice to the criminal complaint filed by SEBI in the NSEL matter and/or any proceedings pending before any authority in respect of similar matter concerning the Noticee or other relevant persons.
58. A copy of this order shall be served upon the Noticee and the recognized Market Infrastructure Institutions for necessary compliance.

**Sd/-**

**DATE: JULY 20, 2023**

**PLACE: MUMBAI**

**S.V. MURALI DHAR RAO**

**EXECUTIVE DIRECTOR**

**SECURITIES AND EXCHANGE BOARD OF INDIA**