QJA/GG/MIRSD/DOP/29065/2023-24

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.
Karvy Comtrade Limited	**INZ000073335**

In the matter of National Spot Exchange Limited

BACKGROUND

1. Securities and Exchange Board of India (hereinafter referred as the **"SEBI"**) had appointed a Designated Authority (hereinafter referred to as the **"DA"**) to enquire into and to submit a report pertaining to the acts of Karvy Comtrade Limited (hereinafter referred to as the **"Noticee"**) as a stock broker, into the possible violations of Regulations 5(e), 9(b) and 9(f) of the SEBI (Stock Brokers) Regulations, 1992 (hereinafter referred to as the **"Stock Brokers Regulations"**) read with Schedule II of the SEBI (Intermediaries) Regulations, 2008 (hereinafter be referred to as the **"Intermediaries Regulations"**), alleged to have been committed by the Noticee in the matter of trading activities on the spot exchange platform provided by the National Spot Exchange Limited (hereinafter referred to as the **"NSEL"**).

2. After conducting the enquiry as envisaged under Regulation 25 of the Intermediaries Regulations, on the basis of material available on record and after considering the replies filed by the Noticee, the DA submitted an enquiry report dated January 27, 2020 (hereinafter referred to as the **"Enquiry Report"**)

in respect of the Noticee in terms of Regulation 27 of the Intermediaries Regulations as it stood at the relevant point of time prior to its amendment vide SEBI (Intermediaries) (Amendment) Regulations, 2021, w.e.f. January 21, 2021, wherein the DA, based on various factual findings and observations so recorded in the Enquiry Report, recommended that the registration of the Noticee as a stock broker may be cancelled. The relevant excerpts of the Enquiry Report are reproduced below:

> *"…*
> *47. 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. Karvy Comtrade Limited [Registration No. INZ000073335] as a commodities derivatives broker may be cancelled."*

3. A Show Cause Notice dated February 12, 2020 (hereinafter referred to as the **"SCN"**) enclosing therewith the Enquiry Report of the DA and certain other documents as specified in the said SCN, was issued to the Noticee under Regulation 28(1) of the Intermediaries Regulations, as applicable at the relevant time, calling upon it to show cause as to why the action of cancellation of Certificate of Registration, as recommended by the DA or any other action as may be considered appropriate by the Competent Authority, should not be taken against it. The SCN further advised the Noticee to submit its reply, if any, within 21 days of receipt of the said SCN. The Noticee filed its reply to the SCN vide letter dated June 04, 2020.

4. While the aforesaid proceedings were pending, SEBI passed five separate orders during February 2019 rejecting the applications filed by five entities (involved therein) seeking 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 the **"SAT"**). Hon'ble SAT, vide its common order dated June 9, 2022, remanded the aforesaid SEBI orders to SEBI to decide these matters afresh

within six months from the date of the order of Hon'ble SAT. While remanding the aforesaid SEBI orders, 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..."*

5. In light of the aforesaid order of Hon'ble SAT and certain other subsequent orders passed by Hon'ble SAT in similar set of cases from time to time, it was felt necessary to furnish certain additional documents/ material to the Noticee before concluding the present proceedings. Accordingly, SEBI, vide a Supplementary Show Cause Notice dated February 13, 2023 (hereinafter referred to as the **"SSCN"**, collectively SCN and SSCN being referred to as **"SCNs"**) provided certain additional documents/ material to the Noticee and advised it to submit its reply/ comments/ clarifications in addition to its earlier replies, if any, within 15 days of receipt of the SSCN. The Noticee was further informed that if no reply is received within 15 days of receipt of the SSCN, it would be presumed that it had no additional comments/ reply to submit and the matter would be proceeded in terms of the provisions contained in the Intermediaries Regulations. In response, the Noticee, vide letter dated May 12, 2023 submitted its reply.

6. It is pertinent to mention that Regulation 27 of the Intermediaries Regulations was amended with effect from January 21, 2021. Pursuant thereto, the procedure for action on receipt of the recommendation of the DA was duly incorporated in the amended Regulation 27 of the Intermediaries Regulations. Thus, these proceedings are being considered under the amended Regulation 27 of the Intermediaries Regulations.

7. In the interest of natural justice, the Noticee was granted an opportunity of personal hearing on May 15, 2023 through video conferencing. On the scheduled

date of hearing, the Authorised Representative of the Noticee appeared and made submissions in line with its earlier replies and sought a weeks' time to file additional written submissions. Thereafter, vide letter dated May 23, 2023, the Noticee submitted its further submissions.

8. As the principles of natural justice have been adhered to in the present matter, it is now a fit case to be proceeded with, on merits, based on the material contained in the SCNs as well as the replies/submissions of the Noticee available on record and the oral submissions made during the personal hearing.

9. The replies filed by the Noticee vide its letters dated June 04, 2020, May 12, 2023 and May 23, 2023, and the oral submissions made during the hearing are summarized hereunder:

(i) SEBI had granted certificate of registration to the Noticee in September 15, 2016, therefore it is perplexing that after granting registration and lapse of so many years SEBI has raked up the allegation regarding fit and proper person.

(ii) During the relevant time i.e., 2010 – 2013, Noticee had executed trades on NSEL both on behalf of clients and also in its proprietary account and out of the outstanding amount of ₹ 34 Crore (approx.) to be received from NSEL, amount to the extent of ₹16 Crore pertains to clients and the remaining amount of around ₹ 18 Crore pertains to the proprietary trades.

(iii) SEBI has not provided all the documents relied upon by it for levelling charges against the Noticee.

(iv) There was irregularity involved in appointment of the DA since the power to appoint a DA has been vested with the Executive Director of SEBI and not with the Whole Time Member of SEBI.

(v) The Noticee has allegedly participated in/ facilitated trading in the paired contracts at the trading platform of NSEL when it was governed by the rules, regulations, bye laws of NSEL and also by the provisions of Forward Contracts (Regulation) Act, 1952 (hereinafter referred to as the **"FCRA"**).

(vi) SEBI is not empowered to investigate/ inquire into the alleged violations of FCRA.

(vii) The letter dated November 20, 2015 of the Ministry of Finance has direct bearing on the question of jurisdiction of SEBI on spot market and since the erstwhile Forward Market Commission (hereinafter referred to as the **"FMC"**) had not dealt/ initiated any action against the brokers, SEBI is not supposed to deal with the matter in question pertaining to the members of NSEL, which is also prohibited as per the said letter of the Ministry of Finance.

(viii) When the commodity brokers were brought under the jurisdiction of SEBI with effect from September 28, 2015, the Finance Act, 2015 inserted a new Section 29A in Securities Contracts (Regulation) Act, 1956 (hereinafter referred to as the "SCRA") in terms whereof a fresh proceeding related to an offence under the FCRA could be initiated by SEBI under the FCRA within a period of three years from the date on which the FCRA is repealed. 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 could not 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 there under.

(ix) SEBI Regulations cannot be made applicable retrospectively.

(x) 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.

(xi) There was no reason to believe that the operations of NSEL were not in accordance with the applicable laws and exemptions granted by the Central Government, and the Central Government never raised any concerns regarding the same.

(xii) The Noticee had not brought in any investor to invest in paired contracts or promised them assured returns and was not aware about the illegality or the alleged paired contracts, counter party sellers, etc.

(xiii) Noticee had not facilitated or financed anyone for the purpose of trading in the paired contracts.

(xiv) Reliance on decisions of the Hon'ble Tribunal in the matter of *Jermyn Capital vs. SEBI* and *Mukesh Babu Securities vs. SEBI* is misplaced since both the matters were decided by Hon'ble SAT to show that close association with any person who does not enjoy a good reputation, is good enough to determine that the person in question is not fit and proper person, however, no such facts are available in the present case since a person holding a Certificate of Registration from SEBI as an intermediary cannot be construed as having close association with the exchange or SEBI merely on the basis of being a member or intermediary.

(xv) The relationship between NSEL and Noticee was that of an exchange and member/ broker and the relationship was at complete arms-length and for the misconduct of the exchange, Noticee cannot be blamed.

(xvi) That there is no close connection between the Noticee and the NSEL since the Noticee do not hold any shareholding, position in the NSEL, nor they played any role in the decision making of NSEL of permitting trading of the alleged paired contracts.

(xvii) The reliance placed by the DA on the adverse observations made by Courts/ Authorities including the Economic Offence Wing, the finding of the DA that the paired contracts were not contracts in commodity but in the form of financial transactions, etc., are not relevant and are devoid of any force in light of the decision of the Hon'ble Bombay High Court in the matter of *63 Moons' Technologies Limited vs. State of Maharashtra* dated August 22, 2019.

(xviii) The Hon'ble High Court in the aforesaid matter has held that the paired contracts were not financial transactions but were trades in commodity as per regulations and bye laws of NSEL.

(xix) If any member of NSEL is found guilty of violating any provision of the FCRA, Regulations and bye laws, the member may be punished under FCRA and it is not necessary to declare that the member is not a 'fit and proper person'.

(xx) Observations by the Courts/ Agencies/ Authorities on the mismanagement of NSEL by its promoters and key managerial personnel cannot have any

bearing on the 'fit and proper person' status of the Noticee and the Noticee was not a party to the FMC order dated December 17, 2013 wherein the FMC found fault with the operations of NSEL.

(xxi) The report of the Economic Offence Wing does not level any specific charges against the Noticee and the same cannot be relied upon as the same is only an interim investigation report and has to undergo test of judicial scrutiny.

(xxii) The reliance on the interim report of the Economic Offence Wing is misplaced since it does not hold the Noticee responsible for indulging in any of the activities which were investigated by them.

(xxiii) The findings of the DA that the Noticee allowed itself to become an instrument of NSEL by participating in the execution of the alleged 'paired contracts' is perverse and baseless as the 'paired contracts' were introduced by NSEL with the approval of its Board and presented to the public that and brokers that the paired contracts are legal and permissible contract as per Government of India Gazette Notification dated June 05, 2007.

(xxiv) The trades carried by the clients through the Noticee were as per NSEL system from time to time. No brochures, pamphlets, presentations on NSEL products were issued or provided to its clients by the Noticee and the NSEL was functioning in complete public knowledge and the Noticee had no reason to question the legality of 'paired contracts' offered by NSEL.

(xxv) The Government of India's letter dated December 30, 2014 merely confirms the Government's agreement with the view of erstwhile FMC that the NSEL had violated the conditions conferred under Section 27 of the FCRA by the Central Government vide its Notification No. SO 906 (E) dated June 05, 2007 (hereinafter referred to as **"2007 Exemption Notification"**) and the said letter was silent on the activities of the members of the NSEL. Further, the letter is neither an investigation report not a judicial/ quasi-judicial order and cannot be relied upon.

(xxvi) In the Hon'ble Bombay High Court dated January 15, 2020, in Criminal Application in *Moonish Rangari & Ors. vs Union of India*, it was held that the entire jurisdictional basis of the SFIO Investigation which was ordered

by the Central Government in the purported "public interest" vide its Order dated October 28, 2016 has ceased to exist. In view thereof, the SFIO Investigation Report appears to be without jurisdiction. In view of the judgment of the Hon'ble Supreme Court dated April 30, 2019 in the matter of 63 Moons Technologies Limited and the aforesaid Hon'ble High Court of Bombay, the investigation of SFIO is without any jurisdiction and hence cannot be relied upon by SEBI for drawing any adverse inference.

(xxvii) Merely because FIR has been filed by SEBI against the Noticee, which is patently sweeping, vague and lacks any credible basis, no adverse inferences can be drawn against the Noticee.

(xxviii) The disqualifications contained in the amendment to the Schedule II of the Intermediaries Regulations cannot be read and applied mechanically, ignoring the text of the Complaint/ FIR. The allegations levelled therein and the lack of substantiating material for the same.

(xxix) That whether Noticee is named in the chargesheet filed by EOW is of great importance for levelling the charges of not fulfilling the fit and proper criteria against the Noticee.

(xxx) Cancellation or suspension of a certificate of registration is a matter of serious concern and it has far-reaching consequences.

(xxxi) DA has not justified as to how the alleged violations were so egregious or of aggravating in nature, which justifies cancellation.

(xxxii) While recommending the cancellation, the DA has totally ignored and failed to consider the 'principles of proportionality'.

(xxxiii) MCX had declared Noticee as defaulter vide circular dated December 18, 2020 and on the basis of the same, NCDEX had also declared Noticee as defaulter.

CONSIDERATION OF ISSUE AND FINDINGS

10. I have carefully perused the SCNs issued to the Noticee and the enquiry report, the replies dated June 04, 2020, May 12, 2023 and May 23, 2023, and the oral submissions made during the hearing 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 SCNs, 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.

11. Before coming to the merits of the case, it is relevant to deal with the contention of the Noticee that the power to appoint a DA has been vested in the Executive Director, while in the instant case, the DA has been appointed by the Whole Time Member of SEBI thereby raising a concern about the irregularity in the appointment of DA. 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, rank and position to the Executive Director of SEBI, is devoid of any merit.

12. Noticee has also contended that it has not been provided with the relevant documents in the matter necessary for levelling charges against it. I note that Sub-regulation (3) and (4) of Regulation 25 of the Intermediaries Regulations specify that 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. On perusal of the SCNs, Enquiry Report and material/ information available on record, I find that all the documents relied upon by SEBI for levelling charges against the Noticee have been provided to the Noticee along with the SCN and SSCN. I note that Noticee, in its replies, has not mentioned anywhere the list of relevant documents which it intends to seek or inspect. Also, during the personal hearing, Noticee did not submit before me that it has not been provided with the relevant documents in the matter. Thus, I find that all the necessary documents relied upon by SEBI for framing charges against the Noticee have been provided to it.

Therefore, the principles of natural justice have been adhered to while conducting the proceedings under the Intermediaries Regulations.

13. Noticee has also submitted that the investigation of SFIO is without any jurisdiction and cannot be relied upon by SEBI for drawing any adverse inference. In this regard, I note that the SFIO Investigation Report was not the relevant document which has been relied upon for issuance of the SCNs.

14. Before I proceed to examine the issue, as stated above, *vis-à-vis* the material available on record before me, it would be appropriate at this stage, to refer to the relevant 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.

The 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, -
(a)…..
(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;

The 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.

15. I note that prior to merger of FMC with SEBI on September 28, 2015, the Noticee was required to be a member of an association recognised by the Central Government under Section 6 of the FCRA, and 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 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".*

16. I note that pursuant to the merger of FMC with SEBI, a commodity derivatives broker was mandatorily required to obtain a certification 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 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 September 15, 2016 and since then it has been acting as a market intermediary registered with SEBI.

17. Noticee has argued that SEBI has no power or jurisdiction to investigate/ inquire into the alleged violations of the FCRA. 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. I note that Section 29A of FCRA, as inserted by the Finance Act, 2015*, inter alia,* provides –

"(1) The Forward Contracts (Regulation) Act, 1952 is hereby repealed.
(2) On and from the date of repeal of Forward Contracts Act–
(a)….
…….
(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."

18. I note that the aforesaid provision empowers SEBI to initiate a fresh proceeding with respect to the offences under FCRA within a period of three years from the date on which FCRA was 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 Economic Offence Wing (hereinafter referred to as 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, the aforesaid proceedings are different from the proceedings before me. 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 the EOW under Section 154 of the Code of Criminal Procedure, 1973 (hereinafter referred to as **"CrPC"**). The Noticee is obligated to maintain the fit and proper person criteria on a continuous basis, and it is well within SEBI's jurisdiction and powers to adjudge the said fit and proper status of the market intermediaries in the interest of securities market.

19. I note from the SCN that Noticee was called upon to show cause as to why the information/ material as brought out in the SCN and in the Enquiry Report concerning fit and proper person criteria should not be considered for determining the fit and proper status of the Noticee. Subsequently, a SSCN, enclosing a copy of the order passed by Hon'ble SAT on June 9, 2022, as mentioned at paragraph 4 above, (hereinafter referred to as **"SAT Order"**), was issued to the Noticee calling upon the Noticee to show cause why the following information/ material along with the Enquiry Report should not be considered against it for determining whether the Noticee satisfies the '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 (hereinafter referred to as the **"FIR"**) dated September 28, 2018; and
    c. Amended Schedule II of the Intermediaries Regulations.

20. As regards other observations in Hon'ble SAT's Order, I find that the present matter in hand is different from that of those 5 cases as in the extant matter the Noticee is already holding a Certificate of Registration whereas in those 5 cases, the entities had filed applications seeking certificate of registration, which were pending at the time of passing those orders.

21. Before moving forward to consider the matter on merits and 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 19 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. INZ000073335 with effect from September 15, 2016 and was stated to be a member of the Multi Commodity Exchange of India Limited, National Commodity and Derivatives Exchange Limited and National Multi-Commodity Exchange of India Limited.

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 FCRA, the Central Government vide its 2007 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 prescribed under the said 2007 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 different spot exchanges, including NSEL in the prescribed reporting formats. After analyzing the trade data received from the NSEL, FMC passed Order No. 4/5/2013-MKT-1/B dated December 17, 2013 in the matter (hereinafter referred to as the **"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 the 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, while granting exemptions to the one day forwards contract for sale and purchase of commodities traded on the NSEL, from the purview of the FCRA.

22. I note that to initiate proceedings under the Intermediaries Regulations for ascertaining the fit and proper status of the Noticee, it is not a pre-condition that the Noticee should be party to the FMC Order. The reliance on the FMC Order is to cognize the nature of contracts being traded on the NSEL and violations of the relevant provisions of law in order to ascertain the fit and proper status of the Noticee in the securities market. 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 2007 Exemption Notification were violated:

a. <u>Short Sale</u>

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. <u>Contracts with Settlement Period going beyond 11 days</u>

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 2007 Exemption Notification.

23. 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 2007 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 2007 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.

24. 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:

> *"….. 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".*

25. Noticee has submitted that the paired contracts were not financial transactions but were trades in commodity as per regulations and bye laws of NSEL. I find

this submission of Noticee untenable in light of the judgement 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"**), wherein the Hon'ble Supreme Court while drawing reference to the representations made by the 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."*

26. 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. At Para 45 of 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. It was also noted in 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 short sales i.e., commodities to back such sales were not available at the designated warehouses of the NSEL.

27. I note that, the total amount to be received by the Noticee as per the EOW report is ₹ 34,46,10,656. In this regard, Noticee has submitted that during the relevant time i.e. 2010 – 2013, it had executed trades on NSEL both on behalf of clients and also in its proprietary account and out of the outstanding amount of ₹ 34 Crore (approx.) to be received from NSEL, amount to the extent of ₹ 16 Crore pertains to clients and the remaining amount of around ₹ 18 Crore pertains to the proprietary trades.

28. I note that the Noticee in its submissions has, *inter alia*, stated that the finding of the DA that the Noticee allowed itself to become an instrument of NSEL by participating in the execution of the alleged 'paired contracts' is perverse and baseless as the 'paired contracts' were introduced by NSEL with the approval of its Board and presented to the public that and brokers that the paired contracts are legal and permissible contracts as per Government of India Gazette Notification dated June 05, 2007. Noticee has further submitted that the trades carried by the clients through the Noticee were as per NSEL system from time to time and that the NSEL was functioning in complete public knowledge and the Noticee had no reason to question the legality of 'paired contracts' offered by NSEL. Noticee has also submitted that no reliance can be placed on the EOW report since it does not hold the Noticee responsible for indulging in any activities which were investigated by them. Noticee further submitted that the relationship between NSEL and Noticee was that of an exchange and member/ broker which was at complete arms-length and for the misconduct of the exchange, Noticee cannot be blamed.

29. It is an accepted fact that the Noticee had indulged in paired contracts. Considering the deliberations and discussions recorded above the moot question is whether the Noticee while facilitating transactions in paired contracts for its

clients under the 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. Further, as stated above, NSEL itself was advertising such contracts as an alternative to fixed deposits and the return offered was fixed (e.g. 16%) 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.

30. In the undeniable background that there was a settlement default at NSEL, it is clear 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 contracts 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*.

31. As recorded in the SSCN, it is not in dispute that SEBI has filed a complaint dated September 24, 2018 with EOW, Mumbai, against brokers who facilitated access to 'paired contracts' traded on NSEL, including the Noticee, On the basis of this complaint, subsequently, an FIR dated September 28, 2018 came to be registered with the MIDC Police Station, Mumbai, against the Noticee, which is subsisting and has not been challenged, quashed or stayed by any competent court *qua* the Noticee.

32. I note from the records that, the Noticee has not provided any explanation to the observation made in the EOW Report wherein, as on the closure of the business of NSEL, the obligation outstanding due to the Noticee was ₹ 34,46,10,656/-. I find that the unsettled obligations of the Noticee, as noted in the EOW Report, evidence that the Noticee allowed itself to become an instrument of NSEL in facilitating trading in 'paired contracts' among its clients.

33. In the background of the aforesaid discussion and deliberation pertaining to 'paired contract' as captured in the preceding paragraphs, I now move on to examine whether the Noticee satisfies the 'fit and proper person' criteria as laid down under Schedule II of the Intermediaries Regulations.

34. Having established that the Noticee has traded in 'paired contracts' for its clients, I now proceed to examine the allegations levelled against the Noticee in the SCNs and the SSCN. It is noted that the main allegation against the Noticee, as levelled in the SCN, is that by facilitating in 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 SSCN, 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 being in violation of Regulation 5(e) of the Stock Brokers Regulations read with Schedule II of the Intermediaries Regulations. 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.

35. Noticee has contended that SEBI Regulations cannot be made applicable retrospectively and 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. In this context, as noted above, the Noticee is holding a Certificate of Registration granted by SEBI on December 17, 2015. 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 a 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. Therefore, 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 the powers to examine the 'fit and proper' status of such entity based on various parameters. Therefore, even if the Noticee was found to have fulfilled the 'fit and proper person' criteria while granting the Certificate of Registration, in 2016, such an intermediary can still be assessed on being fit and proper at a later date.

36. Noticee has argued that SEBI had granted certificate of registration to the Noticee on September 15, 2016 and therefore it is perplexing that after granting certificate of registration and lapse of so many years SEBI has raked up the allegation regarding the fit and proper criteria. In this regard, as already noted that being a 'fit and proper' person, is a continuing 'eligibility criteria'/ statutory requirement, which ought to be satisfied by all registered entities at all points of time and there is no merit in the argument. The principle of estoppel does not apply to the instant case and if the continued applicability of the fit and proper criteria to its functioning is challenged, there would exist a market where the overall interest of the investors would stand compromised. Further, the due presumption on the constitutional and legal validity of the said amended Schedule II of the Intermediaries Regulations holds the field even till date and hence any arguments to the contrary are not maintainable. The Noticee is

obligated to maintain the fit and proper person criteria on a continuous basis and 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 the securities market.

37. Furthermore, 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 as 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*, includes 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;"*

38. In this regard, Noticee has submitted that FIR has been filed by SEBI against the Noticee, which is patently sweeping, vague and lacks any credibility and thus no adverse inference can be drawn against the Noticee. I note from the SSCN that an FIR has been registered with the MIDC Police Station, Mumbai, against the Noticee under section 154 of the CrPC. On September 28, 2018 and the same is pending as on date and is subsisting and has not been challenged, quashed or stayed by any competent court *qua* the Noticee. The disqualifications listed under paragraph 3(b) of the amended criteria of Schedule II of the Intermediaries Regulations are unambiguously clear and no exemptions from such criteria has been provided. Once the disqualification is triggered, the 'fit and proper' person criteria is open for determination by SEBI. It is, therefore, noted that the disqualification provided in paragraph 3(b)(i) under the amended Schedule II of the Intermediaries Regulations is also triggered vis-à-vis the Noticee.

39. It is noted that the Noticee has traded in the 'paired contracts' on behalf of its clients. I note that the Noticee, as a broker and as a member of NSEL, represented NSEL to the regular investors. 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 provide its platform for trading in 'paired contract' that were not permitted under the 2007 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/or dealing in 'paired contracts' which were in the nature of financing transaction (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 clients to the risk involved in trading in a product that did not have regulatory approval thereby raises 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 itself and for its clients on the NSEL platform have serious ingredients jeopardizing the reputation, belief in competence, fairness, honesty, integrity and character of the Noticee in the securities market.

40. I note that when provisions of law specify certain acts to be done in a particular manner, the same is required to be honoured in letter and spirit. Law does not provide any exception to any person to perform such acts that are not permissible under an extant legal framework as per their whims and fancies. Therefore, if an exemption is granted in respect of all forward contracts of one-day duration for the sale and purchase of commodities traded on NSEL from operations of the provisions of the FCRA subject to compliance with certain conditions then it is obligatory on the part of a market intermediary to execute forward contracts of one-day duration only, subject to strict compliance with the said conditions. As noted above, the principle of *'ignorantia juris non excusat'* or that *'ignorance of law is no excuse'* becomes squarely applicable.

41. Thus, while examining the consequences of the conduct of the Noticee, the fact that is undeniably clear to me is that the conduct as has been displayed by the Noticee in its trading on the NSEL platform which was detrimental to the interest

of the investors in the securities market resulted in the filing of a criminal complaint by SEBI. Thus, the Noticee has also incurred the disqualification under Clause 3(b)(i) of the amended provisions of Schedule II of the Intermediaries Regulations on account of the complaint filed by SEBI and the FIR that was registered by the EOW based on the said complaint of SEBI.

42. Given the discussion and deliberations, I am constrained to conclude that the Noticee, presumably driven by its desire to earn brokerage and/ or profit, provided access to its clients to participate in an illegal product, which raises serious questions on its ability to conduct proper and effective due diligence regarding the product itself. Such activities of the Noticee as a registered broker cannot be condoned and deserve appropriate measure to prevent such wrong doings from recurring to the detriment of the interest of the Securities Market.

43. Thus insofar as an FIR against the Noticee under section 154 of CrPC has been registered with the MIDC Police Station, Mumbai which is subsisting/ pending as on date, the Noticee attracts the disqualification provided in paragraph 3(b)(i) under the amended Schedule II of the Intermediaries Regulations. I hold that the Noticee does not satisfy the 'fit and proper person' criteria specified in Schedule II of the Intermediaries Regulations and its continuance as a registered entity in the securities market would be detrimental to the interest of the investors in the securities market.

CONSIDERATION OF THE RECOMMENDATION OF DESIGNATED AUTHORITY

44. I note that the DA has recommended in the Enquiry Report the certificate of registration of the Noticee be cancelled since the Noticee is not a "fit and proper", person. Noticee has submitted that its name is not in the chargesheet filed by EOW and thus the recommendation of the DA is not justified since it failed to consider the 'principles of proportionality'.

45. In this regard, I note that Noticee attracts the disqualification provided in paragraph 3(b)(i) under the amended Schedule II of the Intermediaries Regulations, the Noticee is not a "fit and proper" person. In the interest of the

securities market, once an intermediary is declared to be not "fit and proper," it should not be permitted to continue acting as an intermediary until it has regained its "fit and proper" status. In this context, it is pertinent to mention that in several scenarios, a defect which justifies holding an intermediary as not “fit and proper” may be curable at the hands of the intermediary, while in certain scenarios it is not.

46. In this instance, the Noticee has been determined not to be "fit and proper" for the reason that its conduct, integrity, and reputation have been found wanting as a result of the Noticee's involvement in trading "paired contracts" on the NSEL platform. Additionally, since the FIR dated September 28, 2018 has been registered by EOW, which is still pending for final determination by a Court of competent jurisdiction, the disqualification specified in paragraph 3(b) under the amended Schedule II of the Intermediaries Regulations stands invoked.

47. 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. 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 may 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.

48. In this regard, I note that the question that now arises for determination is whether the certificate of registration of the Noticee should be cancelled or whether it should be suspended for a specific period. A direction of cancellation, even when the EOW charge sheet is the subject matter of *lis* before the MPID Court, would entail the complete winding up of the business of the Noticee. On the other hand, “suspension for a specific period” would serve the purpose of keeping the Noticee

out of the securities market for a specified period, after which the Noticee may resume its business, after curing the issues that have led to such an action.

49. Given the peculiar facts and circumstances of the case, I am of the considered view that a direction of suspension of certificate of registration of the Noticee for a period of three months or till discharge/ acquittal of the Noticee by a Court of competent jurisdiction, whichever is later, would be more appropriate and commensurate to the violations brought out in the present case.

ORDER

50. In view of the foregoing discussions, I, in exercise of powers conferred upon me under Section 12(3) and Section 19 of the SEBI Act read with Regulation 27 of the Intermediaries Regulations suspend the certificate of registration (bearing No. INZ000073335) of the Noticee i.e., Karvy Comtrade Limited for a period of three months from the date of this Order or till an order is passed by a Court of competent jurisdiction discharging or acquitting the Noticee, whichever is later.

51. The Noticee shall, immediately after receipt of this order, inform its existing clients, if any, about the aforesaid direction in paragraph 50.

52. The Order shall come into force with the immediate effect. A copy of this order shall be served upon the Noticee and the recognized Market Infrastructure Institutions for necessary compliance.

Sd/-

Place: Mumbai
Date: August 31, 2023

G P GARG
EXECUTIVE DIRECTOR
SECURITIES AND EXCHANGE BOARD OF INDIA