

SECURITIES AND EXCHANGE BOARD OF INDIA
FINAL ORDER

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

In respect of:

NAME OF THE NOTICEE	CIN	SEBI REGISTRATION NO.
SUNIDHI COMMODITIES PVT. LTD.	U51909MH2003PTC143393	INZ000042837

In the matter of National Spot Exchange Limited

I. Background:

1. Sunidhi Commodities Pvt. Ltd. (hereinafter referred to as "**SCPL**")/ "**Noticee**") is a commodities derivative broker and a member of the Multi Commodity Exchange of India Ltd. (hereinafter referred to as "**MCX**"). SCPL was earlier a Member of the National Spot Exchange Limited (hereinafter referred to as "**NSEL**"). Subsequent to the merger of the Forward Market Commission (hereinafter referred to as "**FMC**") with Securities and Exchange Board of India (hereinafter referred to as "**SEBI**") on September 28, 2015, SCPL registered with SEBI as a trading/clearing member bearing SEBI Registration No. INZ000042837.
2. As a member of the NSEL, the Noticee had participated in / facilitated trading in 'paired contracts' on the NSEL platform, SEBI initiated enquiry proceedings against the Noticee under Chapter V of the SEBI (Intermediaries) Regulations,

2008 (hereinafter referred to as the “**Intermediaries Regulations**”) and appointed a Designated Authority (hereinafter referred to as the “**DA**”) vide order dated September 21, 2018, to enquire into whether the Noticee was a ‘fit and proper person’ (hereinafter referred to as “**FPP**”) to continue to hold the certificate of registration as Trading and Clearing Member in terms of Regulation 5 (e) read with Regulation 27 (iv) of the SEBI (Stock Brokers) Regulations, 1992 (hereinafter referred to as the “**Broker Regulations**”).

II. Brief History of Illegal Forward Contracts on NSEL:

3. Before considering the compliance of the Noticee with the FPP criteria, it would be appropriate to have a preliminary discussion on the background of NSEL which forms the basis of the current proceedings.
4. NSEL was incorporated in 2005 as an exchange for spot trading of commodities. I note from the FMC Order No.4/5/2013-MKT-1/B dated December 17, 2013 (“**FMC Order**”), that on June 05, 2007, the Department of Consumer Affairs (“**DCA**”), Ministry of Consumer Affairs, Food and Public Distribution, Government of India, issued a Notification S.O.906(E) under Section 27 of Forward Contracts (Regulation) Act, 1952 (hereinafter referred to as “**FCRA**”) granting certain exemptions from the provisions of FCRA to NSEL subject to specified conditions. The relevant extract of the said notification is reproduced hereunder for ease of reference:

“...the Central Government exempts all forward contracts of one day duration for the sale and purchase of commodities traded on the National Spot Exchange Limited, from operation of the provisions of the said Act subject to the following conditions, namely:-

- i. no short sale by members of the Exchange should be allowed;*
- ii. all outstanding positions of the trade at the end of the day shall result in delivery;*
- iii. the National Spot Exchange Ltd. shall organize spot trading subject to regulation by the authorities regulating spot trade in the areas where such trading takes place;*

iv. all information or returns relating to the trade as and when asked for shall be provided to the Central Government or its designated agency;

.....”

5. The aforesaid notification was amended on February 6, 2012 by DCA vide Gazette Notification S.O. 228(E) specifying “Forward Markets Commission, Mumbai” as the designated agency of the Central Government.
6. NSEL commenced operations in October 2008. It is seen from the FMC Order and the Judgement dated April 22, 2022 of the Hon’ble Supreme Court, in the matter of The State of Maharashtra Vs. 63 Moons Technologies Ltd, Civil Appeal Nos. 2748-49 of 2022, that NSEL, in September 2009, introduced the concept of ‘paired contracts’, which involved buying and selling the same commodity through two different contracts at two different prices, wherein investors 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 short, 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. “T” indicates the trade date, that is, the date on which the trade took place; and +2 or +3 or +25 or +36, indicates the number of business days after the trading day when the delivery of the commodity and the payment of price ought to have been made. The transactions were structured in a manner that the buyer of the short duration contract always ended up making profits.
7. Further, from Para 8 of the FMC Order, I note that the DCA on April 27, 2012 directed NSEL to explain as to why action should not be initiated against NSEL for violation of the conditions of the notification dated June 05, 2007. In response to the same, NSEL submitted a reply vide their letter dated May 29,

2012. DCA, vide its letter dated May 31, 2012, sought comments of the FMC on the NSEL reply. The FMC, vide its letter dated August 02, 2012 to the DCA provided its comments on the two main issues, which are relevant for consideration of the matter at hand, as paraphrased hereunder:

(i) Short Sale by members of the Exchange: NSEL did not insist upon ownership of goods before allowing its members to place the sale order. FMC was of the view that all those sale transactions which are not backed by the ownership of goods were in violation of the condition of *"no short sale by the members of the Exchange shall be allowed"*.

(ii) Contracts in which settlement period goes beyond 11 days: In view of the definition of forward contract under FCRA, FMC was of the view that all the contracts traded on NSEL which provide settlement schedule for a period exceeding 11 days are Non-Transferable Specific Delivery contracts. Thus, even if the gazette notification does not specify the delivery period, NSEL had to settle the delivery for all open position within a period of 11 days as NSEL was allowed to only trade in one- day forward contracts and was obliged to ensure delivery and settlement within 11 days.

8. I also note from Para 8 of the FMC Order that DCA, vide its letter dated July 12, 2013, directed NSEL to give an undertaking that:

(i) *No further/ fresh contracts shall be launched by NSEL until further instructions from the concerned authority; and*

(ii) *All the existing contracts will be settled on the due dates.*

9. To sum up, as per the original notification dated June 05, 2007, NSEL was granted conditional exemption from the provisions of FCRA for all forward contracts of one-day duration for the purchase and sale of commodities. The two main conditions were that (i) there should be no short sale and (ii) all outstanding positions at the end of the day should result in delivery. Thereafter, FMC had observed that 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 provisions of FCRA. 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”. In view of the said definition contained in FCRA, 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.

10. NSEL, thus, had permitted contracts of various commodities having duration longer than 11 days and these contracts were *ex facie* in contravention of the exemption granted to NSEL vide the Government Notification dated June 05, 2007. Further, I note that the Hon’ble Supreme Court, in its Judgement dated April 22, 2022 in the matter of The State of Maharashtra Vs. 63 Moons Technologies Ltd, Civil Appeal Nos. 2748-49 of 2022, while drawing reference to the presentations made by NSEL in respect of ‘paired contracts’ had *inter alia* held that:

“44.... NSEL in the course of its brochures has held out representations about the trading and investment opportunities available for:

- a) corporate clients*
- b) high net worth individuals; and*
- c) retail investors*

45. Under the head of “contract specifications”, the following representation has been held out :

<i>Commodity</i>	<i>Duration</i>	<i>Investment (lacs.)</i>	<i>Yield</i>
<i>Castor Seed</i>	<i>T+3 & T+36</i>	<i>7.5 -9 Lacs</i>	<i>16%</i>
<i>Castor Oil</i>	<i>T+5 & T+30</i>	<i>7-9</i>	<i>16%</i>
<i>Cotton Wash Oil</i>	<i>T+2 & T+25</i>	<i>10</i>	<i>16%</i>
<i>Paddy</i>	<i>T+2 & T+25</i>	<i>3.5-4.5</i>	<i>16%</i>
<i>Steel</i>	<i>T+2 & T+25</i>	<i>4.5-5</i>	<i>16%</i>

Raw Wool	T+2 & T+25	3.5-4	16%
Wool Top	T+2 & T+25	1.8-2	16%
Crude Soybean Oil	T+2 & T+25	3.3.-3.5	16%
Soya DOC	T+2 & T+25	1.7-2.0	16%
Refined Mustard Oil	T+2 & T+25	6.5	16%
Refined Soybean Oil	T+2 & T+25	6.5	16%
Refined Sunflower Oil	T+2 & T+25	6.5	16%
RBD Palmolein Oil	T+2 & T+25	6.5	16%
Sugar	T+2 & T+25	3.0	16%
Maize	T+2 & T+25	3.0	16%

The above representation specifies:

- (i) Commodities;*
- (ii) Duration of trades;*
- (iii) Investment; and*
- (iv) Yield.*

For example, in the case of castor seeds, NSEL held out a buy contract (T+3) and sale contract (T+36), in which the yield is stated to be 16%. Moreover, NSEL represented that:

“Opportunities

- Traders can trade and lock their return*
- Trader has to buy in near settlement contract and sell in far settlement contract simultaneously*
- Price for both settlement available*
- Exchange provides counterparty guarantee risk*
- No basis risk, No link with future contracts*

While describing the features of trading opportunity, NSEL represented that:

“Features of Trading Opportunity:

- *T+2 and T+25 contract offers unique trading opportunity to traders*
- *Trader purchases T+2 contract and simultaneously sells T+25 contract*
- *Pay-in obligation is on T+2 while Pay-out of the funds will be on T+25. Entire settlement cycle is of 35-37 days*
- *Price differential between the two settlement dates i.e premium if annualized offers interest rate of about 16%*
- *Income arising out of such trades are treated as Business Income”*

While comparing the investment opportunities of bank fixed deposits with trading opportunities at NSEL, NSEL represented that:

“Comparison

- *Bank FD 9.25% for 390 days; NSEL Trading Opportunity 16%;*
- *Bank FD minimum duration 390 days; NSEL Trade duration 35-55 days, depending on the contract*
- *Traders have an option of rolling over their position as per their convenience*

.....

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."

11. As such, both the FMC Order and the aforesaid order of Hon'ble Supreme Court have explicitly brought out the details as to how NSEL permitted short sales - i.e. by permitting sellers to offer contract for sale of commodities on its platform without ensuring that requisite amount of commodity is available in the warehouse.
12. It is also pertinent to note that the Hon'ble Supreme Court in another Judgement dated April 30, 2019, titled 63 Moons Technologies Ltd Vs. Union of India, Civil Appeal No. 4476 of 2019 observed that these contracts were in the nature of "financing transactions". The relevant extract of the said order is as under: -

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

III. Show Cause Notice, Reply and Hearing

13. In light of the background and history narrated above, the DA issued show cause notice dated September 25, 2018 (hereinafter referred to as the "**SCN**") to the Noticee, calling upon it show cause as to why it should be found to be not "fit and proper person" in terms of Regulation 5(e) read with Regulation 27 of the Broker Regulations and Schedule II of the Intermediaries Regulations and hence, liable for cancellation of its registration. Vide letter dated October

25, 2018, the Noticee sought extension of time to file its reply. Vide letter dated November 02, 2018, the Noticee submitted its reply to the said SCN. Subsequently, the Noticee vide letter dated November 13, 2019 submitted details of paired contracts executed by it during the period September 2009 to August 2013. Upon completion of the enquiry, the DA submitted its report dated November 20, 2019, recommending cancellation of the certificate of registration granted to the Noticee since it was not a FPP.

14. Pursuant to the same, a post enquiry show cause notice (hereinafter referred to as the “**SCN-1**”) dated January 15, 2020, was issued to the Noticee, under Regulation 28(1) of the Intermediaries Regulations to show cause as to why action, as recommended by the DA or any other action as considered appropriate by the Competent Authority, should not be taken against the Noticee. A copy of the DA’s Report was also forwarded to the Noticee along with an advice to file a reply, if any, within 21 days from the date of receipt of the notice. Along with the DA’s Report, the letter dated December 30, 2014 of the Ministry of Finance (“**MoF**”), Department of Economic Affairs (“**DEA**”) addressed to the Chairman, FMC was provided to the Noticee, wherein it was stated that the DEA was in agreement that NSEL had violated the conditions of exemptions granted to it under the FCRA. Further, Order dated August 22, 2014 of Hon’ble Bombay High Court, in the matter of *Jignesh Prakash Shah Vs. The State of Maharashtra*, Criminal Bail Application No. 1263 of 2014, wherein it was held that the brokers through whom the paired contracts were entered into had knowledge of the illegality of such contracts, was also furnished to the Noticee. The SCN-1 also *inter alia* highlighted the observations made by the Hon’ble Supreme Court in the matter of *63 Moons Technologies Ltd. Vs. Union of India* (order dated April 30, 2019), wherein it was held that paired contracts were in fact financing transactions in breach of exemptions granted to NSEL under the FCRA. The Noticee was also called upon to show cause as to why information/materials as brought out therein along with the DA’s Report should not be considered. The Noticee submitted its reply to the

SCN-1 vide letter dated June 01, 2021 which contained submissions on lines of its reply dated November 02, 2018.

15. In the meantime, while the proceedings in the present matter were ongoing, Whole Time Member, SEBI (“**WTM**”) passed certain orders rejecting the applications of five other entities for registration as commodity brokers. The Hon'ble Securities Appellate Tribunal (“**the Hon'ble SAT**”) vide its order dated June 9, 2022 remitted the matters to the WTM to decide the matter afresh after giving an opportunity of hearing to the brokers. Further, Hon'ble SAT had 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 SEBI 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*”.
16. In light of the order of Hon'ble SAT dated June 9, 2022, a supplementary show-cause notice dated October 07, 2022 (hereinafter referred to as “**SCN-2**”) was issued to the Noticee. Vide the SCN-2, additional documents viz. SEBI's complaint dated September 24, 2018 to Economic Offence Wing (“EOW”), First Information Report (“FIR”) dated September 28, 2018 and the amended Schedule II of the Intermediaries Regulations were furnished to the Noticee calling upon it to show cause as to why information/material provided therein along with the Enquiry Report should not be considered against the Noticee.
17. In response to the SCN-2, the Noticee vide letter dated October 21, 2022 acknowledged receipt of the SCN-2 and submitted that it has no comments to offer whether the Competent Authority should consider the information/material brought on record vide the SCN-2.
18. In order to proceed with the matter, a hearing was granted to the Noticee in terms of Regulation 27(4) of the Intermediaries Regulations, 2008 as the DA

had recommended cancellation of the certificate of registration of the Noticee. The hearing was held on December 06, 2022, during which Anil Shah, Advocate, along with Mahesh Desai, Compliance Officer of the Noticee, appeared for the Noticee and reiterated the submissions made in replies dated November 02, 2018, November 13, 2019 and June 01, 2021.

19. The summary of the Noticee`s replies dated November 02, 2018, June 01, 2021 and additional submissions dated December 16, 2022 is given hereunder:

- (i) The SCN is vague and ambiguous and is based on the observations set out in the enquiry report dated November 20, 2019. The allegations therein are not specific and definite. Reliance is placed on observations of the Hon`ble Supreme Court of India in the matter of Commissioner of Central Excise Vs. Brindavan Beverages (P) Ltd, (2007) 5 SCC 388 and Canara Bank & Ors Vs. Debasis Das & Ors, [(2003) 4 SCC 557].
- (ii) The documents relied on by SEBI while arriving at findings against it have neither been provided to it nor is there any mention of these documents in the SCN. Reliance is placed on the Hon`ble Supreme Court Judgment in the matter of Securities and exchange Board of India Vs. Price Waterhouse (Civil Appeal No. 6003-6004/12).
- (iii) It denied that it had participated and/ or facilitated its clients in trading on the NSEL in such paired contracts during the period September 2009 to August 2013.
- (iv) As per FMC order No. 4/5/2013- MKT-I/B dated December 17, 2013, it was NSEL who was responsible for conducting its business not in accordance with the conditions stipulated in the notification dated 05.06.2007 granting it exemption from the operation of FCRA, 1952, with regard to the one-day forward contracts to be traded on its exchange platform and violating the condition of 'no short-sell' and 'compulsory

delivery of outstanding position at the end of the day' stipulated in the notification.

- (v) During the period September, 2009 to August, 2013, it entered into only three paired contracts, one each on behalf of its clients viz., Watermark Financial Consultants Limited, Watermark Systems (India) Private Limited and another on behalf of its group company Sunidhi Capital Pvt. Ltd, in accordance with their instructions.
- (vi) On 06.01.2010, it entered into paired contract on behalf of its group company Sunidhi Capital Pvt Ltd. which stood duly settled on 08.02.2010. It entered the said contracts in normal course of business to check the functioning of the Spot Exchange by entering only into single contract. It has not done any trade on proprietary accounts. On 20.07.2011, it entered a paired contract under the instructions and on behalf of its clients viz., Watermark Financial Consultants Limited and Watermark Systems (India) Private Limited which stood duly settled on 13.09.2011.
- (vii) Till passing of order dated December 17, 2013, it had no reason to suspect that the above paired contracts were in contravention of provisions of the FCRA and the Central Government Notification dated June 05, 2007 as concluded therein. Till passing of the said order dated December 17, 2013 neither had FMC nor any other Regulatory Authority raised any objection/ warning/ caution that the alleged paired contracts were in contravention to the provisions of FCRA and government notification dated 05.06.2007 and consequently in violation of Regulation 9(b), 9(f) read with Clause A (1), A(2) and A(5) of the Schedule II and 5 (e) of the Brokers Regulations read with Schedule II of the Intermediaries Regulations.
- (viii) NSEL had assured the contracting parties on the NSEL platform that the trades shall be settled and in case of a default from either of the contracting parties the responsibility shall lie with NSEL to clear and settle all traded

contracts on NSEL as per NSELs Rules, Bye laws and Regulations and the Settlement Guarantee Fund.

- (ix) As a commodity broker, it has exercised proper due diligence at the time of registration of the client by knowing the client. It has taken all care, which is required to be taken about the creditability and financial soundness of its clients and subsequently ensuring that contracts are not fictitious and that contracts were duly settled as per NSEL norms.
- (x) It has maintained high standards of integrity, promptitude and fairness in the conduct of its broking business and has duly abided by all the provisions of the Act, the Rules, Regulations and Bye laws and guidelines issued by the Government, the Board and the Stock Exchange from time to time as may be applicable to it and Code of Conduct as specified in Schedule II of the Brokers Regulations. It has acted only as an intermediary/ facilitator to earn brokerage. It has executed trades on behalf of and under the instructions of its clients as it ought to have as a commodity broker.
- (xi) As a broker, it was impossible for the Noticee to identify that contracts of its clients were ultimately in the nature of financial transactions and therefore, in contravention to the provisions of FCRA and Government notification dated 05.06.2007 and consequently in violation of Regulation 9(b), 9(f) read with Clause A (1), A (2) and A(5) of the Schedule II and 5 (e) of the Brokers Regulations read with Schedule II of the Intermediaries Regulations. Reliance is placed on the order dated June 20, 2006, passed by the SAT in Kasat Securities Private Ltd. Vs. Securities and Exchange Board of India and the judgment of the Hon`ble High Court of Bombay in the matter of Tri Sure India Ltd. Vs. A.F. Ferguson and Co. & Others.
- (xii) Its principal officers and the key management persons and company are indeed persons of high integrity, reputation and character. No conviction

or restraint orders have been passed against its principal officers and the key management persons. It has never been categorized as a willful defaulter. Its principal officers and the key management persons and company are competent in all aspect of commodity trading including financial solvency and net worth and thus duly fulfill the requirements of criteria for determining a 'fit and proper person' as specified vide Schedule II of the Intermediaries Regulations, 2008.

- (xiii) It has not resorted to any mis-selling of contracts as the contracts were in accordance with the conditions and stipulations offered on the NSEL trading platform and it had no role to play in the same since the NSEL had been recognized under the FCRA and MCA had jurisdiction to regulate contracts and their validity and implementation. It had adhered to all the Rules, Bye Laws and Regulations of NSEL and that it was never issued any SCN by the NSEL. There were no complaints against it from any client.
- (xiv) SEBI Regulations were not applicable to it at the relevant time when the paired contracts were executed. At the relevant time, trades were governed by the Bye laws and Business Rules of NSEL and circulars issued by NSEL. SEBI Regulations were not applicable to the members of NSEL.
- (xv) Upon repeal of FCRA on September 28, 2015 by the Finance Act, 2015, undertaking of FMC was transferred to and vested with SEBI and SEBI was made regulator for the commodities market and the members of commodities exchange. With a view to govern the members of commodities exchanges like that of recognized stock exchanges, the Broker Regulations were amended and made applicable to the commodities brokers to be registered with SEBI with effect from September 29, 2015. 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. SEBI Regulations cannot be made applicable retrospectively.

- (xvi) Bye law 4.1 of NSEL Bye laws authorized the Board of the Managing Director or the committee so appointed to finalize contract specification and modifications and it had no role to play in the same. Thus, it was not required to assess legality of the product introduced by the NSEL. Bye law No. 4.2 of NSEL mandated it to execute and clear transactions in only such contracts as specified by the Board. Further, Bye law No. 4.5 mandated that all transactions in commodities permitted on the Exchange shall be made only in the manner approved by the Exchange. Thus, it could not have traded in the paired contracts which were otherwise not violative of Bye law No. 4.2 and 4.5 of NSEL.
- (xvii) 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 with the provisions of FCRA.
- (xviii) Cancellation of registration certificate is proposed to be made in respect of all members of NSEL irrespective of the number or value of trades entered into by them in the alleged paired contracts. Levying proposed punishment uniformly defies the doctrine of proportionality.
- (xix) Reliance on FMC order is misconceived and misplaced as it was not party to the said order.
- (xx) Hon`ble Bombay High Court in its judgment dated August 22, 2019 in the matter of 63 Moons Technologies Ltd. Vs. State of Maharashtra held that paired contracts were not financial transactions but were trades in

commodity as per regulations and bye laws of NSEL and rejected following contentions of the State Government: -

- a. In paired contracts, money was received by NSEL from investors and it was passed on to the borrowers of NSEL.
- b. Entire transaction was a financial transaction with assured fixed returns to the investors.
- c. NSEL is covered within the fold of the definition of financial establishment attracting provisions of MPID Act.

(xxi) The said judgment dated August 22, 2019 has rendered following contentions of SEBI as irrelevant: -

- a. The paired contracts were not contracts in commodity but in the form of financial transactions;
- b. Adverse observations made by various courts/competent authorities against NSEL and paired contracts have seriously impacted the reputation of NSEL and paired contracts;
- c. The Noticee facilitated the trading in paired contracts and hence was closely associated with NSEL and paired contracts;and
- d. Adverse observations made by courts/authorities including EOW can be taken into account for determining the fit and proper criteria.

(xxii) Pursuant to SEBI complaint dated September 24, 2018, FIR No. SPL LAC No. 110/18 dated September 28, 2018 was registered by Economic Offences Wing ("EOW") at MIDC Police Station. Its name is at Sr. No. 237 in the said FIR. SIT-EOW has filed final charge sheet before the Hon'ble Sessions Court, Mumbai, Court No. 52, CF No. 23615/2003, wherein, it has been made a witness at Sr. No. 192 of the witness list. It supposes

that charge-sheet in the matter has been filed on December 02, 2022 or December 05, 2022.

20. Further, the Noticee vide reply dated November 13, 2019 provided details of paired contracts executed by it which is as follows: -

Table-1

Trade Date	Settlement date	Client Name	Commodity Name	Buy qty	Sell qty	Trade Value
06-01-10	09-01-10	Sunidhi Capital Pvt. Ltd	Cottonseed Wash Oil	12	-	2,520,660
06-01-10	08-02-10	Sunidhi Capital Pvt. Ltd	Cottonseed Wash Oil	-	12	2,548,740
20-07-11	25-07-11	Watermark Financial Consultants Limited	Castor Seed	900	-	3,090,385
20-07-11	13-09-11	Watermark Financial Consultants Limited	Castor Seed	-	900	3,156,772
20-07-11	25-07-11	Watermark Systems (India) Private Limited	Castor Seed	1800	-	6,180,570
20-07-11	13-09-11	Watermark Systems (India) Private Limited	Castor Seed	-	1800	6,313,545

21. Subsequently, the Noticee vide letter dated February 22, 2023 submitted an affidavit, executed by its compliance officer-Mahesh Desai, affirming the said contention regarding filing of FIR No. SPL LAC No.110/18 dated September 28, 2018 at MIDC Police Station and filing of final charge sheet by EOW-Mumbai(NSEL-SIT) before the Hon`ble Sessions Court, Mumbai, Court No.52, bearing CF no. 23615/2022. It is stated that neither the Noticee nor any of its employee has been charge sheeted as an accused in the said case.

IV. Consideration of Issues

22. I have considered the SCN, SCN-1, SCN-2, the Enquiry Report submitted by the DA, replies and submissions of the Noticee and other material available on record. Having regard to the same, I now proceed to deal with the issues in the present matter.
23. It is alleged that the Noticee, being member of NSEL participated and/or facilitated its clients in executing paired contracts, has violated Regulation 5(e), 9(b) and 9(f) read with Clause A(1), A(2) and A(5) of the Schedule II of the Broker Regulations read with Schedule II of the Intermediaries Regulations. The relevant provisions are reproduced hereunder: -

Provisions of 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

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.*

Provisions of 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-clauses (b) and (c) of clause (2) comply with the 'fit and proper person' criteria."

24. From the reply of the Noticee, it is seen that the Noticee has admitted to the fact of execution of the illegal contracts, referred to as "paired contracts" by FMC and the Hon'ble Supreme Court, on behalf of its clients on NSEL. Further, the Noticee has stated that it entered into paired contract under instructions and on behalf of its clients. Further, the Noticee has submitted that NSEL was responsible for conducting its business not in accordance with conditions stipulated in the notification dated June 05, 2007. The Noticee has attempted to shift the entire burden for the illegality underlying the trades onto NSEL and the other regulators who were supposed to supervise. In short, it is contended that there was no reason for the Noticee to suspect the paired contracts or the functioning of NSEL. I have also taken note of the fact that the Noticee has relied on NSE Bye Laws to contend that it was mandated to execute and clear transactions in paired contracts. I find that the Noticee was well aware that the duration of the contracts exceeded one day which was stipulated as one of the conditions of exemption notification. I note from the reply of the Noticee that the Noticee executed 3 paired contracts during September 2009 to August 2013. On perusal of reply of the Noticee, I find that the Noticee had sufficient experience in dealing with other commodity exchanges such as National Commodity & Derivatives Exchange Ltd. ("**NCDEX**"), MCX, etc. As a broker with sufficient experience and knowledge and having presence in various other exchanges and in different markets, the Noticee ought to have refrained from participating on the subject contracts or from allowing its clients to participate on such platform, going by the very structure of the back-to-back contracts. It appears to be the case of the Noticee that since everything was in public domain and it was all being done with the knowledge of regulators, it presumed that the activities were legally valid and that there was nothing that raised his suspicion. In this context, I note that NSEL itself was advertising such contracts

as an alternative to fixed deposits. The return offered was 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 of short term contract always made pre-determined profits. I am, therefore, of the view that while executing trades for clients in such contracts, the Noticee failed to examine the basic nature of the product and also failed in understanding the source of powers relied upon by NSEL for selling such products which other exchanges were not offering. Thus, the Noticee failed to conduct proper and effective due diligence on these aspects of paired contracts which were not essentially spot contracts.

25. I note that the SCN -1 mentioned observations made by the Hon`ble Supreme Court in its order dated April 30, 2019, in the matter of *63 Moons Technologies Limited (Formerly known as 'Financial Technologies India Limited) & Ors. Vs. Union of India & Ors, Civil Appeal No. 4476 of 2019*. Further, the SCN-1 enclosed Enquiry Report dated November 20, 2019, copies of DEA letter dated December 30, 2014 and 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* and the Noticee was called upon to show cause as to why information/material brought therein should not be considered along with Enquiry Report. I note that the Hon'ble SAT, in its order dated June 09, 2022, in respect of the applications of five other entities for registration as commodity brokers, has held that the observations in the bail rejection order of the Hon'ble Bombay High Court cannot be relied upon as the observations therein are limited to the fact as to whether the bail should be granted or not. Accordingly, I find that 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*, is not relevant for consideration in the present matter. Further, I note that the Bombay High Court Judgment dated August 22, 2019 was set aside by the Hon`ble Supreme Court vide its judgment dated April 22, 2022, in the matter of *The State of Maharashtra Vs. 63 Moons Technologies Ltd, Civil Appeal No.*

2748 of 2022. In view thereof, I find that reliance placed by the Noticee on the Judgment dated August 22, 2019 is misplaced.

26. I note that the Noticee has stated that the SCN-1 is vague, ambiguous and based on the observations set out in the Enquiry Report dated November 20, 2019. Further, it is stated that the allegations therein are not specific and definite. I note that the SCN alleged that paired contracts executed on NSEL were in contravention of provisions of FCRA and the Central Government Notification dated June 05, 2007. Further, it alleged that the Noticee, a member of NSEL and a SEBI registered trading and/or clearing member under the Brokers Regulations, had participated and/or facilitated its clients in trading on the NSEL in such paired contracts during the period of September 2009 to August 2013 and thereby, the Noticee violated Regulation 9(b), 9(f) read with Clause A(1), A(2) and A(5) of the Schedule II and 5(e) of the Brokers Regulations read with Schedule II of the Intermediaries Regulations. The SCN -1 enclosed Enquiry Report dated November 20, 2019, DEA letter dated December 30, 2014 and Hon`ble Bombay High Court order dated August 22, 2014 and the Noticee was called upon to show cause information/material brought out in the SCN-1 along with the Enquiry Report should not be considered and why action recommended by the DA or any other action should not be taken against the Noticee. In view of the above, I find that the SCN detailed acts and omissions of the Noticee and provisions of law alleged to be violated by the Noticee. I do not agree with the contention of the Noticee that the SCN is vague or ambiguous or did not contain specific allegations. I, therefore, find that reliance placed by the Noticee on observations made by the Hon`ble Supreme Court in the matter of Commissioner of Central Excise Vs. Brindavan Beverages (P) Ltd, (2007) 5 SCC 388, and Canara Bank & Ors. Vs. Debasis Das & Ors, (2003) 4 SCC 557 is inappropriate and irrelevant.
27. I note that the Noticee has stated that documents relied upon by SEBI or the DA for arriving at findings against it have not been provided to it. I note that the Noticee in response to the SCN-1 filed reply dated June 01, 2021 which

repeated submissions made vide its reply dated November 02, 2018. I find that the Noticee`s reply dated June 01, 2021 did not contain any reason as to why the information/material brought in the SCN-1 should not be considered. I find that documents relied upon have been provided to the Noticee vide SCN-1 and SCN-2.

28. I note that the Noticee has placed reliance on following observations made by the Hon`ble Supreme Court in its order dated January 10, 2017 in the matter of Securities and Exchange Board of India Vs. Price Waterhouse, Civil Appeal No. 6003-6004/12: -

“We direct, that all statements recorded during the course of investigation shall be provided to the respondents. We further direct, that all documents collected during investigation shall be permitted to be inspected by the respondents. The authors of such statements (recorded during investigation), which are to be relied upon (against the respondents), shall be offered for cross-examination to the respondents. Only thereupon, it will be permissible to rely upon the same.

29. I note that Hon`ble Supreme Court in the said order dated January 10, 2017 also noted that *“Having heard learned counsel for the rival parties, we find no justification to examine the matter in detail. We wish to dispose of this case with some simple clarifications”*. In view of the said observations, Hon`ble Supreme Court made observations relied upon by the Noticee. I note that the principle enunciated in the said order dated January 10, 2017 is that statements recorded during the course of investigation can be relied upon only when the other party has been provided with copy of the statements and opportunity to cross examine the maker of the statements. In the present case, no such statements are being relied upon. I find that the said order dated January 10, 2017 is not applicable to the present case.

30. I note that the Noticee has also contended that it was bound by Clauses 4.1 and 4.2 of NSEL Bye laws according to which the contract specifications and

modifications were finalized and executed. As such, NSEL activities itself were being investigated and the concerned authorities including the Hon`ble Supreme Court have given adverse findings about the activities of NSEL. It is, therefore, not open to the Noticee to rely on the same.

31. I note that the Noticee has also contended that cancellation of registration certificate is proposed to be made in respect of all members of NSEL irrespective of the number or value of trades entered into by them in the alleged paired contracts and therefore is not in accordance with the doctrine of proportionality. As the matter pertains to ascertaining of the FPP criteria of the brokers, I do not find it appropriate to apply the test of severability or proportionality to the tainted contracts.
32. I note that Schedule II of the Intermediaries Regulations was amended vide SEBI(Intermediaries) (Third Amendment) Regulations, 2021, w.e.f. 17.11.2021 and the following disqualifications have been included amongst others:
“(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;”
33. I note that vide the SCN-2, additional documents viz. SEBI's complaint dated September 24, 2018 to EOW, FIR dated September 28, 2018 and the amended Schedule II of the Intermediaries Regulations was provided to the Noticee. Further, the Noticee was called upon to show cause as to why the information/material brought out in the SCN-2 along with the Enquiry Report dated November 20, 2019 should not be considered against it. In response thereto, the Noticee vide letter dated October 21, 2022 submitted that it has no comments to offer whether the Competent Authority should consider the information/material brought on record vide the said SCN.
34. I also note that as per the amendment, the disqualification of an associate or group entity of the applicant or intermediary of the nature as referred to in sub-clause (b) of clause (3) of Schedule II to the Intermediaries Regulations, shall

not have any bearing on the FPP 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.

35. It is pertinent to note that in terms of Regulation 5(e) of Broker Regulations, the eligibility criteria for an entity to get registered as a stock broker includes that it should be a 'fit and proper person' based on the criteria specified in Schedule II of Intermediaries Regulations. I note that the Noticee has contended that SEBI Regulations cannot be made applicable to it as alleged acts pertain to period prior to September 28, 2015. I note that Section 28A of FCRA provided that a person buying or selling or otherwise dealing in commodity derivatives as a commodity derivatives broker or such other intermediary who may be associated with the commodity derivatives market, immediately before transfer and vesting of rights and assets to SEBI for which no registration certificate was necessary prior to such transfer may continue to do so for a period of 3 months from such transfer or, if he has made an application for such registration within the said period of three months, till the disposal of such application. Accordingly, the Noticee applied for registration as a broker and was granted the same. Since then, it has been acting as market intermediary registered with SEBI. It has been specified in Clause 7 of Schedule II of Intermediaries Regulations that FPP criteria is required to be satisfied by the intermediary at the time of registration as well as during the continuity of registration with SEBI. Therefore, even assuming that Intermediaries Regulations and the Brokers Regulations were not applicable to the Noticee at the time of execution of pair contract but after September 28, 2015, the Noticee is obligated to comply with FPP criteria on continuous basis.
36. The Noticee has placed reliance on the order dated June 20, 2006, passed by the SAT in the matter of Kasat Securities Private Ltd. Vs. SEBI, wherein, it has been observed "*... that merely because the appellant acted as a broker cannot lead us to the conclusion that it must have known about the nature of the transaction. There has to be some other material on the record to prove this*

fact.” I note that allegations in the said case were that i) the Appellant therein had aided and abetted its clients in executing the manipulative and fraudulent transactions and thereby failed to exercise due skill and care; and (ii) it failed to collect margins from its clients when it traded on their behalf. Hon`ble SAT in the said order dated June 20, 2006 also observed that *“There is no material on record to show that the appellant as a broker knew that the trades were fictitious or that the buyer and the seller were the same persons..... Therefore, it was not possible for the broker to know who the parties were. Merely because the appellant acted as a broker cannot lead us to the conclusion that it must have known about the nature of the transaction”*. However, in the present case NSEL itself was advertising such contracts as an alternative to fixed deposits. The return offered was 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. Therefore, in the present case, there were enough red flags for the Noticee to know that the said paired contracts were impermissible and illegal. Accordingly, I find that the said order dated June 20, 2006 is distinguishable on facts and is not applicable to the present case.

37. The Noticee has also placed reliance on the judgment of the Hon`ble High Court, Bombay in the matter of Tri-Sure India Ltd. Vs. A.F. Ferguson and Co. & Others, wherein, it has been observed that *“It is well-established law that it is sufficient if one exercises the ordinary skill of an ordinary competent man exercising that particular art. It hardly requires to be stated that the burden to prove any action of negligence rest primarily on the plaintiff who, to maintain the action, must show that he was injured by the negligent act or omission for which the defendant in law, is responsible.”* I find that the said judgment is distinguishable on facts as well as law and is not applicable to facts of the present case.
38. It is a matter of record that SEBI has filed a complaint dated September 24, 2018 with EOW seeking appropriate action under Sections 20 and 21 and other

applicable provisions of FCRA against the brokers/members of NSEL, mentioned in the list attached thereto. I note that the Noticee is listed at serial no. 237 in the said list. Pursuant to the SEBI complaint, FIR No. Spl LAC No. 110/18 dated September 28, 2018 under section 154 of the Code of Criminal Procedure, 1973 has been registered at the MIDC Police Station, Mumbai against the same trading members, which were listed in the SEBI complaint to EOW. I note that the said FIR is currently pending. In view thereof, I note that disqualifications contained in paragraph 3(b)(i) of Schedule II of Intermediaries Regulations are attracted against the Noticee.

39. When the pendency of a criminal complaint or FIR filed by SEBI is prescribed as a negative criterion / disqualification from eligibility under Schedule II of the Intermediaries Regulations, it is imperative for me to consider the same while adjudging the eligibility of the Noticee to continue to hold the authorization granted. In my view, the amendment of Schedule II of the Intermediaries Regulations merely encapsulates the criteria in the form of distinctly identifiable parameters, which would apply uniformly to all intermediaries. To reiterate, the fact that SEBI has filed a complaint and FIR has been registered against the Noticee and the same is pending, in itself constitutes a disqualification from satisfaction of eligibility criteria to function as an intermediary.
40. I note that the Noticee has contended that SIT-EOW has filed final charge sheet before the Hon`ble Sessions Court, Mumbai, Court No.52, CF No.23615/2022, where it has been made a witness at Sr. No.192 of the witness list. Further, it is contended by the Noticee that neither the Noticee nor its employee have been arrayed as accused in the said charge sheet. In support of the said contention, the Noticee has filed affidavit dated February 22, 2023. The affidavit also states that the certified copy of the above final charge sheet has been obtained from the Hon`ble Sessions Court, Mumbai by SEBI. The Noticee has not annexed copy of charge sheet stated to have been filed by EOW. I note that EOW has filed charge sheets in FIR No. 89/2013 registered on the

complaint of one Pankaj Saraf. However, FIR lodged by EOW on the complaint of SEBI is Spl LAC No. 110/18 dated September 28, 2018 which is still pending.

41. The evaluation of the facts and legal provisions as brought out above, compels me to arrive at the conclusion that the Noticee is not a 'fit and proper' person and hence is not eligible to continue its business as a stock broker using the certificate of registration no. INZ000042837 granted by SEBI.

DIRECTIONS

42. In exercise of powers conferred upon me under Section 19 read with Section 12(3) of the SEBI Act, 1992 and Regulation 27 of the Intermediaries Regulations, 2008, I, hereby, cancel the Certificate of Registration bearing no. INZ000042837 of the Noticee i.e. Sunidhi Commodities Private Limited.
43. Upon receipt of this order, the Noticee shall immediately inform its existing clients, if any, about the direction at paragraph 42 above.
44. Notwithstanding the direction at paragraph 42 above,
- (i) 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 within a period of next 15 days thereon, under advise to the said clients; and
 - (ii) The Noticee shall square off open positions, if any, within 30 days from the date of this order.
45. This order shall come into force with immediate effect.

46. A copy of this order shall be served upon the Noticee and the recognized Stock Exchanges, Depositories and Clearing Corporations for necessary compliance.

Date: March 31, 2023

Place: Mumbai

Sd/-

GEETHA G

CHIEF GENERAL MANAGER

SECURITIES AND EXCHANGE BOARD OF INDIA