QJA/ARB/MIRSD/DOP/26351/2023-24

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 –

Sr. No.	Name of the Noticee	SEBI Registration No.	PAN
1.	Skung Commxperts Limited	INZ000022932	AAOCS2486D

In the matter of National Spot Exchange Limited

BACKGROUND

1. The present proceedings originate from the Enquiry Report dated November 14, 2019, submitted by the Designated Authority (hereinafter referred to as "**DA**") in terms of regulation 27 of the SEBI (Intermediaries) Regulations, 2008 (hereafter referred to as "**Intermediaries Regulations**") as applicable at the relevant point in time. The DA, based on the facts noted in the said enquiry report, has recommended that the registration of Skung Commxperts Limited (hereinafter referred to as "**noticee**") as a stock broker bearing registration No. INZ000022932 may be cancelled.

2. In this regard, a DA was appointed to enquire into and to submit a report pertaining to the acts of the noticee and into the possible violations of regulations 5(e), 9(b) and 9(f) of the SEBI (Stock Brokers) Regulations, 1992 (hereinafter referred to as "**Stock Brokers Regulations**") read with Schedule II of the Intermediaries Regulations, alleged to have been committed by the noticee.

3. 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 November 14, 2019 (hereinafter referred to as '**Enquiry Report**') in respect of the noticee and found that the noticee, as a stock broker of the National Spot Exchange Limited (hereinafter referred to as "**NSEL**"), had

dealt/facilitated in the trading of the *'paired contracts'* on the exchange platform of NSEL, which was in violation of the applicable provisions of erstwhile Forward Contracts (Regulation) Act, 1952 (hereinafter referred to as "**FCRA**") and the conditions specified in the Government of India Notification dated June 05, 2007 (hereinafter referred to as "**2007 Exemption Notification**"). It was also observed in the Enquiry Report that the continuance of the Certificate of Registration of the noticee as a stock broker (having Registration No. INZ000022932) is detrimental to the interest of the securities market and that the noticee is not a 'fit and proper person' to hold the Certificate of Registration No. INZ000022932 as a stock broker in the Securities Markets which is one of the conditions for grant/holding/ continuance of registration, in terms of regulations 5(e), 9(b) and 9(f) of the Stock Brokers Regulations read with Schedule II of the Intermediaries Regulations. The DA, in view of the aforesaid finding, has recommended that the Certificate of Registration of the noticee as a trading/ clearing member may be cancelled.

4. The relevant excerpt of the Enquiry Report is reproduced below:

   "46. In view of the facts and circumstances of the case and material available on records, it is determined that the Noticee is not a fit and proper person in terms of Regulation 5(e) of the Stock Broker Regulations read with Schedule II of the Intermediaries Regulations. Therefore, in terms of Regulation 27 of the Intermediaries Regulations, it is recommended that the certificate of registration of the Noticee i.e. Skung Commxperts Limited., registered with SEBI as a trading/ clearing member bearing Registration No. INZ000022932 may be cancelled, in the interest of the securities market."

5. Pursuant to the same, a Post Enquiry Show Cause Notice dated January 15, 2020 (hereinafter referred to as "**SCN**") enclosing therewith the Enquiry Report of the DA and certain other material/information 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, in terms of regulation 28(2) of the Intermediaries Regulations (as applicable at the relevant time). 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 vide letter dated February 22, 2020.

6. Meanwhile, SEBI passed five separate orders rejecting the applications filed by five other entities for registration as commodity brokers in the NSEL matter. Aggrieved by the said SEBI orders, the entities filed separate appeals before the Hon'ble Securities Appellate Tribunal (hereinafter referred to as "**Hon'ble SAT**"). The Hon'ble SAT vide 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 said SAT order. While remanding the aforesaid SEBI orders, the Hon'ble SAT *inter alia* held as under:

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

7. In light of the aforesaid SAT order and certain other subsequent orders passed by the 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 Supplementary SCN dated October 11, 2022 (hereinafter referred to as "**SSCN**" and collectively SCN and SSCN being referred to as "**SCNs**") provided certain additional documents/material (as indicated in the SSCN) 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. The SSCN was sent to the noticee through *Speed Post Acknowledgement Due* (for short '**SPAD**') vide letter dated October 11, 2022 and also through email dated October 14, 2022 and proof of delivery of the same to the noticee is on record. However, the noticee did not file its reply to the SSCN.

8. Thereafter, the noticee was provided an opportunity of personal hearing on November 1, 2022. On the scheduled date of hearing, which was held through video conferencing, Mr. Nimish K Somani, Director of the noticee, along with Mr. Ravi Ramaiya, Authorised Representative of the noticee appeared and requested for twenty-one days' time to file the reply to the SSCN and rescheduling the hearing. The request of the noticee was acceded to and accordingly the hearing was rescheduled to November 22, 2022. Subsequently, vide email dated November 21, 2022, the noticee filed its reply to the SSCN. On the said date of hearing, Mr. Nimish K Somani, Director of the noticee, along with Mr. Ravi Ramaiya, Authorised Representative of the noticee appeared and made submissions in line with its earlier replies. While responding to the SSCN dated October 11, 2022, the noticee in its reply dated November 21, 2022 has requested to read its reply in conjunction with its earlier reply dated February 22, 2020. Further, the noticee was granted time till December 2, 2022 for making post hearing submissions, if any. However, the noticee did not make any additional submissions. Thus, the principles of natural justice have been adhered to in the present matter. The matter is fit to be proceeded with, on merit, based on the materials contained in the SCN and SSCN as well as the replies of the noticee available on record.

9. The replies filed by the noticee vide its letters dated September 30, 2019, February 22, 2020 and November 21, 2022, the oral submissions made during the course of the personal hearing held on November 22, 2022, are summarized hereunder:

   i. The notice has been issued barely few days before the completion of the 3 years from the repeal of FCRA. Further, the DA was appointed on September 24, 2018 and the notice was issued on September 25, 2018 which shows that the DA has not considered if there were sufficient grounds to issue the said notice. Therefore, the notice has been issued in haste to the noticee;

   ii. SEBI does not have power and jurisdiction to regulate the spot market in India. The said contention can be corroborated by the "*Report of Expert Committee on Integration of Commodity Spot and Derivatives Markets*" which has observed that spot contracts for commodities are not within the ambit of SCRA and SEBI may be made the regulating authority for the same only after necessary changes to the SCRA;

iii. Till date no competent authority having jurisdiction has held the noticee to be in violation of the provisions of the FCRA and unless the noticee is held liable for allegedly participating/ facilitating in pair contracts by a competent authority, SEBI cannot question the integrity of the noticee;

iv. Pursuant to the merger of SEBI with the FMC, SEBI has amended the Stock Broker Regulations and the Securities Contracts (Regulation) (Stock Exchange and Clearing Corporations) Regulations, 2012 but the said amendment empowers SEBI to regulate only the commodities market and SEBI does not have the power to regulate the spot market even after amendment of the said regulations;

v. The DA has been appointed by the Whole Time Member in the present matter, which is not in accordance with regulation 24(2) of the Intermediaries Regulations, which stipulates that the DA has to be appointed by the Executive Director;

vi. Since the noticee has raised the issue of jurisdiction, the same needs to be decided as a preliminary issue before proceeding further in the matter;

vii. The notice issued to the noticee is vague in nature and therefore it is not valid in the eyes of law as it does not provide details relating to the allegation levied in the notice, the notice does not show that how it is that the noticee participated/ facilitated in the pair contracts or how the noticee was in cahoots with NSEL or its clients, no material including the investigation report etc. has been provided to the noticee, notice is silent on the aspect if the noticee has carried out the trades only on behalf of its clients or also in its proprietary account, etc. Accordingly, the noticee is unable to figure out as to what it is expected to answer;

viii. The noticee has not been provided with the relevant documents as is stipulated in regulation 25(3) of the Intermediaries Regulations. The noticee has not been provided with the trade log and order log of the scrip/ contracts during the investigation period and in the absence of the same, it is not possible for the noticee to provide any justification for its trades whatsoever;

ix. The documents sought by the noticee vide its letter dated October 12, 2018 were not provided in toto by the DA due to which the noticee cannot submit a comprehensive reply. The noticee has been provided with the relevant extracts of Grant Thornton Report and EoW Report but in order to determine the veracity of the documents, the noticee should be provided a cross-examination of the authors of the said reports;

x. The terms 'fails' and 'contravenes', as used in regulation 23 of the Intermediaries Regulations imply that the said provision is only applicable when the default is committed by the person after obtaining the registration with SEBI. The noticee was granted the Certificate of Registration on February 11, 2016 implying that the noticee was a '*fit and proper*' person as on date. Thus, SEBI cannot change its stance and noticee cannot be held liable for any alleged wrong committed before February 11, 2016;

xi. The noticee cannot be held liable solely on the basis of trading in pair contracts, in absence of evidence showing collusion/ malice on the part of the noticee. It is a legitimate expectation of a stock broker that the products introduced by the exchange must be legal and valid and the broker cannot be suspicious of the conduct of the exchange;

xii. The commodities contracts, including the '*paired contracts*' were introduced by Board/ Management of NSEL with prior concurrence of FMC and the noticee was under the impression that if the products are being launched after concurrence of the FMC then the same must be legal and genuine;

xiii. The liability can be fastened on either the exchange for launch of any illegal contract or on the clients for trading and the noticee cannot be held liable for merely acting as the agent of the clients and the exchange;

xiv. No material has been placed on record to suggest any negligence or connivance on the part of the noticee and it is simply stated that the noticee has participated/ facilitated in the '*paired contracts*';

xv. Reliance is placed on the decision of the Hon'ble SAT in the case of *Kasat Securities Private Limited Vs. SEBI* to submit that merely because the noticee acted as broker, it does not follow that the noticee was a party to the game plan of the client in executing the matched trades;

xvi. The noticee cannot be held liable for violation of provisions of Intermediaries Regulations or Brokers Regulations till the clients of the noticee who actually traded in the '*paired contracts*' are held liable as the mischief done by the clients is the pre-requisite to prove the alleged mischief done by the noticee;

xvii. The noticee was not never associated with NSEL or the alleged '*paired contracts*' and it was merely carrying out its duties as broker;

xviii. The dealing/ transactions done by the noticee prior to September 2015 are beyond the scrutiny of SEBI as the regulations under the SEBI Act were not applicable till September 28, 2015 as there was no requirement for the noticee to seek any registration under any law with any statutory author;

xix. There can be no enquiry for the period up to February 2016 as the SEBI Regulations became applicable upon the noticee only after February 11, 2016. Further, no action has been taken by FMC for the relevant period of September 2009 to August 2013 against the noticee and SEBI has not initiated any action under the repealed FCRA;

xx. The noticee has not been duly provided with all the documents and the ones provided by SEBI do not clearly establish the involvement of noticee in the matter. Even the DA has mentioned in the Enquiry Report that the documents provided by the Operational Department of SEBI and the ones provided to the noticee are general in nature and no trade details have been provided by the Operational Department in the NSEL matter which furthers the contention of the noticee that without providing the data pertaining to the trades, the noticee cannot be asked to justify its trading;

xxi. The Grant Thornton Report cannot be relied upon as the noticee has not been provided with the complete copy of the same and only a single line excerpt of Annexure 6 which mentions the payout obligation of NSEL towards noticee has been provided. Thus, in absence of an explanation/ interpretation as to what these figures mean and how they've been arrived at, the noticee cannot proved a defence/ justification of any trading;

xxii. The noticee has not been provided with complete copy of the interim EoW Report rather only a single line excerpt has been provided to the noticee and in the absence of any explanation/ interpretation as regard these figures, the noticee cannot submit a proper defense/ justification;

xxiii. The NSEL circulars dated August 27, 2013 and March 10, 2015 show the payout amounts of the noticee but has nowhere it has been stated that the said payout was for '*paired contracts*' and the fact that the name of the noticee was appearing in the said circulars does not prove or show that the noticee was trading in '*paired contracts*';

xxiv. The noticee, being a broker and trading member, was acting as an agent of the NSEL and was therefore bound to follow the directions and instructions of its principal and hence cannot be held liable or answerable for the alleged wrongdoings of its principal, i.e., its clients and NSEL;

xxv. Reliance cannot be placed on the letter of Department of Economic Affairs dated December 30, 2014 as in the said letter observations have been made only against NSEL and not the noticee;

xxvi. Since the present proceedings have been initiated under SEBI Act/ Intermediaries Regulations, the same are liable to be rendered infructuous as the same are in contradiction with Section 29A(d) of the FCRA which stipulates that all offences committed or existing proceedings shall be continued to be governed by the provisions of FCRA and thus the present proceedings under the Intermediaries Regulations are erroneous and ill-placed;

xxvii. Reliance cannot be placed on the decision of the Hon'ble Supreme Court in the matter of *63 Moons technologies Limited Vs. Union of India* (Appeal No. 4476 of 2019) decided on April 03, 2019 as the noticee has not been made a party to the said order;

xxviii. Reliance is placed by the noticee on the decision of the Hon'ble Bombay High Court in the matter of *63 Moons Technologies Limited Vs. Union of India* (Writ Petition 2743 of 2014) decided on December

4, 2017 to submit that the noticee cannot be held liable for any fraud perpetrated by NSEL without establishing active participation of the noticee in the alleged fraud;

xxix. Reliance cannot be placed on observations of FMC, Hon'ble Bombay High Court and EoW as the noticee was not a party to these proceedings. Further, the observations by the aforesaid authorities are *in rem*, i.e., general in nature and do not pertain specifically to the conduct of the noticee;

xxx. The reliability/ fitness of the observations by EoW and FMC have not yet been tested before any competent authority and therefore, they cannot be relied upon in the present matter;

xxxi. Reliance cannot be placed on interim EoW report for the reasons that no specific allegations have been made against the noticee and that the noticee has not been provided an opportunity to cross-examine the author of the interim EoW Report;

xxxii. Any reliance on the FIR would in gross violation of principles of natural justice as the same is merely a first instance of reporting of complaint based on one sided statements and is far from final determination;

xxxiii. SEBI cannot be permitted to use its own FIR as evidence in a proceeding before it as the said document shows that a complaint has been filed by SEBI and nothing further;

xxxiv. Regulation 5 of the Brokers Regulations stipulates that the SEBI considers the fit and proper person status while considering the application for grant of registration which has already been done in the present case and therefore the allegation purporting to declare the noticee as not fit and proper is *ex facie* untenable and ought to be dropped;

xxxv. Reliance is placed on the decision of the Hon'ble Supreme Court in the matter of *SEBI Vs. Rakhi Trading* to submit that the noticee cannot be held liable for merely facilitating a transaction and there has to be material on record to suggest negligence or connivance on the part of the noticee;

xxxvi. The present regulatory mechanism of SEBI for cash, derivative and commodity derivative segments does not require the noticee to check the legality of the contract/ scrip being traded on the exchange;

xxxvii. The amendment of the criteria for fit and proper person laid out in Schedule II of the Intermediaries Regulations came in effect from November 17, 2021, i.e., much after the initiation of the present proceedings and therefore the same cannot be applied retrospectively;

CONSIDERATION OF ISSUE AND FINDINGS

10. I have carefully perused the SCNs issued to the noticee, the Enquiry Report, the replies dated September 30, 2019, February 22, 2020 and November 21, 2022 filed by the noticee, the oral submissions made on behalf of the noticee during the course of the personal 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 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 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 the 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 reference:

THE 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, -

(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 and Sub-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.

(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.

Liability for action under the Enquiry Proceeding Regulations.

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;

<u>THE INTERMEDIARIES REGULATIONS, 2008</u>

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.

12. Before coming to the merit of the case, it is relevant to deal with the preliminary contention of the noticee that the power to appoint a Designated Authority (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 the

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 sans any merit.

13. The noticee has further contended that SEBI does not have power and jurisdiction to regulate the Spot Market. In this regard, without going into the merits of the contention that whether SEBI has the authority to regulate Spot Market or not, I note, that the issue under consideration in the present proceedings is limited to the determination of "*fit and proper"* status of the noticee under the Intermediaries Regulations. It is a settled position of law that SEBI has statutory authority to determine the "*fit and proper"* status of the intermediaries registered with it. Since the noticee is an intermediary registered with SEBI, I am of the considered view that SEBI is within its jurisdiction to determine the "*fit and proper"* status of the noticee.

14. In any case, SEBI had filed a complaint dated September 24, 2018 with the concerned police authorities for initiating appropriate action for the violations of the provisions of FCRA *inter alia* alleged to have been committed by the noticee. I also note from the records that on the basis of the said complaint of SEBI, a FIR dated September 28, 2018 was registered with MIDC Police Station, Mumbai and the same is validly subsisting. In the background of these facts, it is pertinent to see the scope and scheme of Section 29A(2)(e) of the FCRA which is reproduced as under for ease of reference:

    *"**29A. Repeal and savings. —** (1) The Forward Contracts (Regulation) Act, 1952 (74 of 1952) is hereby repealed.*

    (2) On and from the date of repeal of Forward Contracts Act—

    (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;"

A bare perusal of the aforesaid provision would reveal that it is an enabling provision which enables SEBI to initiate fresh proceedings within a period of three years from the date on which the FCRA is repealed. As stated above, SEBI has *inter alia* filed complaint against the *Noticee* within the stipulated period as specified in the FCRA. Accordingly, I note that SEBI has taken appropriate steps for the alleged violation of the provisions of the FCRA. Therefore, I am of the considered view that the preliminary issue (pertaining to jurisdiction of SEBI) has no force and merit and is accordingly rejected. Further, the contention of the noticee that transactions done by the noticee prior to September, 2015 are beyond the regulatory ambit of SEBI is also misplaced as Section 29A(2)(e) of the FCRA mandates SEBI to initiate appropriate proceedings within the given timeframe for the offences committed under the FCRA.

15. The noticee has also submitted that the documents sought by the noticee vide letter dated October 12, 2018 were not provided *in toto* by the DA due to which the noticee cannot submit a comprehensive reply. Further, the noticee has been provided with the relevant extracts of Grant Thornton (hereinafter referred to as **"GT"**) Report and EoW Report but in order to determine the veracity of the documents, the noticee should be provided a cross-examination of the authors of the said reports. To such a protest, I note that the noticee has not shown any specific prejudice that may have been caused to it in the absence of cross examination of the authors of GT and EOW Reports. Moreover, the noticee has not spelt out reasons/basis for doubting the veracity of the said reports. It therefore, appears that the noticee has merely taken 'cross examination' as an *alibi,* only to avoid its onus to prove its innocence, if any, by producing any evidence whatsoever to defend its case. The plea for cross examination is merely an evasive tactic adopted by the noticee. Further, as regards the submission that the entire Grant Thornton and the interim EOW reports have not been provided to the noticee also does not merit any consideration as the relevant portion of the said reports containing the payout obligation of the noticee has been duly provided to the noticee. In any case, I am of the view that since the said documents are not being relied upon in the present proceedings against the noticee, the need to supply the same does not arise. Accordingly, submissions of the noticee are not tenable.

16. The noticee has further contended that it has not been provided with the trade log and order log of the scrip/ contracts during the investigation

period and in the absence of the same, it is not possible for the noticee to provide any justification for its trades whatsoever. Notably, all the relevant and relied upon documents pertaining to the instant proceedings were provided to the noticee as annexure to the SCNs. In any case it is noticee's own contention that it was trading in the commodities contracts including alleged *'paired contracts'* on behalf of its clients as the said contracts were specified by the Board of NSEL for trading on the exchange. The noticee has further forcefully argued that to hold noticee liable, it must be proved that the noticee had participated in the illegal contracts knowingly and merely executing trades on behalf of the clients will not make the noticee liable. Thus, as per the admissions of the *Noticee* in its reply, it is clear that the *Noticee* has indulged into trading in '*paired contracts*' on behalf of its clients. In these circumstances, the contention that in the absence of trade and order logs, providing the justification for the said trades is not possible, lacks any merit and accordingly rejected.

17. I note that prior to merger of FMC with SEBI on September 28, 2015, the noticee was required to be a member of recognized commodity derivative exchanges 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 thus were not under control of any competent authority, rectified the same through the Finance Act, 2015 by bringing them under the regulatory supervision of SEBI. In this regard, it is also noted that 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 as under:

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

found that the activities of intermediaries dealing in commodity derivatives should not remain uncontrolled and they should be brought under the control of competent authority".

18. Thus, it is an admitted position that prior to the date of merger of FMC with SEBI (i.e. September 28, 2015), the noticee was not required to be registered under the FCRA or any other regulation to act as a commodity derivatives broker. However, after the merger of FMC with SEBI, a commodity derivatives broker was mandatorily needed to have a certificate of registration from SEBI in case it sought to remain associated with the securities market as a commodity derivatives broker. It is seen that the Finance Act, 2015 (as notified on May 14, 2015) conferred the power of regulation over intermediaries dealing in commodity derivatives to SEBI and also mandated regulation of commodity derivatives brokers by SEBI, 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 commodity derivatives market under the erstwhile FCRA but did not require a registration certificate earlier, 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 *w.e.f.* February 11, 2016 and since then it has been acting as a market intermediary registered with SEBI.

19. In light of the order passed by the Hon'ble SAT on June 09 2022, as mentioned at paragraph 6 above (hereinafter referred to as "**SAT Order**") in the NSEL matters, a SSCN dated October 11, 2022 enclosing a copy of the SAT Order was issued to the noticee calling upon the noticee to show cause as to why the following information/material along with the enquiry report dated November 14, 2019 should not be considered against it for determining whether the noticee satisfies '*fit and proper person*' criteria as laid down under Schedule II of the Intermediaries Regulations:

    a. SEBI complaint dated September 24, 2018 filed with Economic Offence Wing ('**EOW**');
    b. First Information Report ('**FIR**') dated September 28, 2018; and
    c. Amended Schedule II of the Intermediaries Regulations.

20. 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:

   i. The noticee, Skung Commxperts Limited, is a commodity derivatives broker registered with SEBI having Registration No. INZ000022932 with effect from February 11, 2016 and is currently a member of the Multi Commodity Exchange of India Ltd. (hereinafter referred to as "**MCX**").

   ii. 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*".

   iii. NSEL was granted conditional exemption from the provisions of the FCRA by the Department of Consumer Affairs, Ministry of Consumer Affairs (for short "**MCA**"), Food and Public Distribution, Government of India, vide Gazette Notification No. S0906(E) dated June 05, 2007, in exercise of the powers conferred under Section 27 of the FCRA, for (i) forward contracts, (ii) for sale and purchase of the commodities, of one–day duration, traded on NSEL subject to certain conditions which, *inter alia*, included that '*no short sale by members of the NSEL shall be allowed*' and that all '*outstanding positions of the trade at the end of the day shall result in delivery*'. It was also stipulated that all information or returns relating to the trade as and when asked for shall be provided to the Central Government or its designated agency.

   iv. In October 2008, the 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 the NSEL had 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 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 contract always ended up making profits.

v. On February 06, 2012, the erstwhile 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 NSEL, FMC passed Order No. 4/5/2013-MKT-1/B dated December 17, 2013 in the matter (hereinafter referred to as "FMC Order") wherein it was inter alia observed that 55 contracts offered for trade on the NSEL platform were in violation of the relevant provisions of the FCRA and that the condition of *'no short sale by members of the exchange shall be allowed'* was being not complied with by 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.

21. 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. Short Sale

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

b. <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.

22. In this regard, the relevant observations of the FMC as recorded in its Order dated December 17, 2013 and also captured in the Enquiry Report are reproduced as under:

"….a large number of NSEL exchange trades were carried out with paired back-to-back contracts. Investors simultaneously entered into a "short term buy contract" (e.g. T+2 — i.e. 2 day settlement) and a "long term sell contract" (e.g. T + 25 i.e. 25 day settlement). The contracts were taken by the same parties at a pre-determined price and always registering a profit on the long-term positions. Thus, there existed a financing business where a fixed rate of return was guaranteed on investing in certain products on the NSEL....."

<u>NSEL conducted 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</u>, with regard to the one-day forward contracts to be traded on its exchange platform. As noted in the SCN, the condition of 'no short-sell' and 'compulsory delivery of outstanding position at the end of the day' stipulated in the notification were violated by NSEL. NSEL Board allowed launching of paired back-to-back contracts on its exchange platform comprising a short-term buy contract (T+2 settlement) and a long-term sell contract (T+25 settlement) with predetermined price and profit for the buyer and seller, <u>which violated the very concept of spot market of commodities and the transactions ultimately were in the nature of financial transactions"</u> (emphasis supplied)

23. It is therefore, clear that the NSEL was given permission to setup as a spot exchange for trading in commodities. It was essentially meant to only offer forward contracts having one-day duration as per 2007 Exemption Notification. I note from the FMC Order that 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. As per the FMC Order 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 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, FMC, in its Order, relying on the definition of "*forward contract*" under FCRA held that NSEL was allowed to trade only in one-day forward contracts and was obliged to ensure delivery and settlement within 11 days. However, it is beyond doubt that 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 the 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. v. Union of India & Others (Civil Appeal No. 4476 of 2019 decided on April 30, 2019)*, wherein it *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. It is also necessary to refer to 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 "**MPID matter**"), wherein the Hon'ble Supreme Court while

drawing reference to the presentations made by the NSEL in respect of the '*paired contracts*' has *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." (emphasis supplied)*

26. Thus, 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 by the Hon'ble Supreme Court that these contracts were in the nature of financing transactions. In the MPID matter (*The State of Maharashtra vs. 63 Moons Technologies Ltd.*), the Hon'ble Supreme Court has held that such transactions come within the definition of '*deposits*' under the MPID Act.

27. 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 a 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 & T+25 paired contract in steel had the same offered return as a T+ 5 & T + 35 paired contract in castor oil. The '*paired contracts'* were being marketed as an alternative to fixed deposits.

28. 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.

29. The aforesaid discussion shows how '*paired contracts'* were not in the nature of spot trading, which was permitted to trade 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 16% p.a. 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. When MCA vide its letter dated July 12, 2013, on the recommendation of FMC, asked NSEL to settle contracts on the due dates and to give an undertaking that no fresh contract shall be launched, NSEL failed to do so and defaulted. Investors lost money as all the underlying warehouse receipts were bogus and there were no underlying securities. As noted in the judgement of the Hon'ble Supreme Court in the MPID matter, the exchange publicized that it provided counter party guarantee risk but, in reality, failed to do so. In view of the above discussion, I note that the submission of the noticee that the aforesaid decisions of the Hon'ble Supreme Court and the observations of FMC order etc., cannot be relied upon as the noticee was not a party to the same, is without any merit as the said decisions have been appropriately relied upon only to highlight the problematic nature of the '*paired contracts*' as observed by the Hon'ble Supreme Court and the FMC order and not to establish any allegation, *per se*, against the noticee. Further, the submission of the noticee that observations of EOW and FMC have not yet been tested by any competent authority and thus cannot be relied upon is misplaced. FMC order dated December 17, 2013 was passed by FMC in terms of section 4 read with section 4A of the FCRA which, *inter alia*, conferred the powers of a civil court upon FMC. Further, the said order has not yet been stayed/ set aside by any appellate authority rather the Hon'ble Bombay High Court vide its order dated February 28, 2014[1], had refused to grant the relief of stay in the matter "*Considering the gravity of the allegations which have been found to be established against the Petitioners,…*". In view of the same and the fact that

[1] Financial Technologies (India) Limited and Ors. Vs. The Forward Markets Commission

the said order is in effect, having not been stayed/ set aside by an appellate authority, the submission that the said order has not yet been tested by a competent authority is not tenable. As regard the EOW report, since the same is not being relied upon in the present proceedings, the need to specifically deal with the submission of the noticee does not arise.

31. On perusal of the replies submitted by the noticee, I note that it is an admitted fact that the noticee had participated/facilitated the execution of *'paired contracts'* for its clients. In this regard, I deem it fit to refer to the submission made by the noticee in its reply dated September 30, 2019 wherein it is *inter alia* admitted at Para 88 that, *"The Noticee was trading in the commodities contracts including alleged paired contracts on behalf of its clients as the said contracts were contracts specified by the Board of NSEL for trading on the exchange"*. Thus, it is an undisputed fact that the noticee has indulged into trading in '*paired contracts*' on behalf of its clients. Since it is an admitted position that the noticee has dealt in the '*paired contracts*' and as the quantum of such dealings is not relevant for the present proceedings, the contentions of the noticee, that the details of the paired trades have not been provided to the noticee or the fact that the noticee was appearing in the NSEL Circulars does not prove that noticee was trading in the '*paired contracts*', are not tenable.

32. In the background of the discussion on '*paired contract*' in the preceding paragraphs, I now proceed to examine whether the noticee satisfies the 'fit and proper person' criteria as laid down under Schedule II of the Intermediaries Regulations.

33. As recorded in the SSCN, SEBI has filed a complaint dated September 24, 2018, against brokers who traded / facilitated access to '*paired contracts'* traded on the NSEL, including the noticee, with the EOW, Mumbai. On the basis of this complaint, an FIR dated September 28, 2018 has also been registered with the MIDC Police Station, Mumbai against the noticee.

34. Having found that the noticee has traded in *'paired contracts'* for its clients, I note that the main allegation against the noticee, as levelled in the SCN, is that by participating/facilitating in the trading in *'paired contracts'* on the NSEL platform during the relevant period as a Trading Member, the noticee has, *prima facie*, violated the conditions stipulated in the 2007 Exemption Notification and consequently the provisions of the FCRA also. Therefore, in the SCN, the noticee was asked to state as to why its certificate of registration

as a commodity derivatives broker, may not be cancelled as the noticee is not a '*fit and proper*' person for holding the certificate of registration. 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 dated October 11, 2022, further alleged that in light of the aforesaid documents as well as observations against the noticee in the enquiry report dated November 14, 2019, the noticee is not a '*fit and proper*' person for holding the certificate of registration.

35. The noticee's main contentions are that the noticee was merely a member of NSEL and followed all the byelaws, rules and regulations of NSEL and noticee was amenable to the regulatory ambit of the NSEL and could not have questioned the competence of NSEL.

36. In this regard, as discussed above, the noticee has admittedly traded in '*paired contracts*' on behalf of its clients. The noticee, as a commodity derivatives broker, represented the face of NSEL for 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 contracts*' that were not permitted under the 2007 Exemption Notification and were purely financial contracts promising assured returns and were advertised as such by NSEL, as observed by the Hon'ble Apex Court, under the garb of spot trading in commodities. Therefore, the noticee by its conduct and as a member of NSEL had promoted and/or dealt in '*paired contracts*' which were in the nature of financing transaction as held by the Hon'ble Supreme Court of India as noted *supra*. The noticee, by providing a platform for taking exposure to '*paired contracts*' exposed its clients, though its group entities, to the risk involved in trading in a product that did not have regulatory approval thereby raising doubts on the competence of the noticee to act as a registered securities market intermediary. As already recorded in SSCN as discussed above, SEBI's complaint dated September 24, 2018 and the FIR registered with the MIDC Police Station, Mumbai on September 28, 2018 under section 154 of Cr.PC is validly subsisting and has not been challenged, quashed or stayed by any competent court *qua* the noticee as on date. Therefore, the noticee attracts the disqualification provided in clause 3(b)(i) of Schedule II of the Intermediaries Regulations.

37. The noticee has also contended that SEBI cannot be permitted to use its own FIR as evidence in a proceeding and that since an FIR is a first instance of reporting of complaint, reliance on the same would be in gross violation of the principles of natural justice. As regard usage of FIR as evidence in the present matter, I note that being a '*fit and proper*' person is a continuing '*eligibility criteria*'/ statutory requirement, which must be satisfied by the noticee including the amended criteria, at all times. I am of the considered view that the due presumption on the constitutional and legal validity of the said amended Schedule II of the Intermediaries Regulations holds the field which is binding upon SEBI, and arguments to the contrary are not maintainable. The noticee has also argued that a FIR or a Criminal Complaint under Section 154 of the CrPC is only the starting point of an investigation and the same cannot be relied upon. To such a protest, I am of the considered view that there is no assertion of guilt made in the SCNs as the present proceedings are for adjudging the continuing '*eligibility criteria'* of *'fit and proper'* status of the noticee. Besides, no material has been brought on record by the noticee to dispute the fact that the said FIR validly subsists as on date. It is neither the case of the noticee that the said FIR has been quashed *qua* the noticee. In the absence of the above discussed factors, I am not inclined to accept the submissions put forth by the noticee in this context.

38. The noticee has contended that the noticee traded in '*paired contracts*' on behalf of the clients as it was specified by the Board of NSEL for trading and the functioning of NSEL was in public knowledge, including the regulatory authorities/ Central Government. Be that as it may, it is noted that the scope of the instant proceeding is not to analyze the actual impact and consequences of the conduct of the noticee but to examine as to whether or not, the noticee has acted in a manner expected of a market intermediary and the answer to the same is clearly against the noticee. For the same reason, the fact whether the name of the noticee was mentioned or not in the FMC order or in the letter dated December 30, 2014 of the Government of India is not relevant. As regards its submission that it was not closely associated with NSEL and the '*paired contracts*' were introduced by NSEL, it cannot be denied that the involvement of the noticee in trading/facilitation of trading in '*paired contracts*' on the NSEL is certainly a conduct which was neither permitted by the 2007 Exemption Notification nor by any of the applicable provisions of the FCRA and

therefore, a conduct similar to that displayed by the noticee in its trading on the NSEL platform would be detrimental to the interest of the Securities Market.

39. It is pertinent to state 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. It is further stated that the '*fit and proper person*' criteria specified in Schedule II of the SEBI (Intermediaries) Regulations, 2008, were amended vide SEBI (Intermediaries) (Third Amendment) Regulations, 2021 with effect from November 17, 2021. The condition of a fit and proper is not a one-time condition applicable only at the time of seeking registration. Rather, as per clause 7 of Schedule II of the Intermediaries Regulations, it is a condition which each and every registered intermediary is required to fulfil on a continuous basis, right from the time of filing such application to the time the entity wishes to remain associated with the Securities Market, as a registered intermediary, after obtaining such registration.

40. It has been argued by the noticee that at the time of grant of Certificate of Registration to the noticee on February 11, 2016, it was already adjudged as a '*fit and proper*' person by SEBI and, therefore, the said criteria are already satisfied by the noticee. The noticee has also submitted that the fit and proper criteria was amended with effect from November 17, 2021, i.e., after initiation of the proceedings against the noticee and thus cannot be applied retrospectively. In this regard, as noted above, the '*fit and proper*' person criteria is a continuing requirement under the Intermediaries Regulations which the noticee ought to comply with at all times as long as it desires to remain associated with the securities market as a registered intermediary. The present proceedings intend to examine the '*fit and proper person*' status of the noticee as per the Intermediaries Regulations. Therefore, I do not find any merit in the arguments of the noticee.

41. At this juncture, I note that the noticee has also contended that SEBI is not empowered to investigate into the alleged violations of FCRA as all offences committed or existing proceedings shall be continued to be governed by provisions of FCRA and thus present proceedings under Intermediaries Regulations are ill-placed. With respect to the same, I note that, SEBI had filed a complaint dated September 24, 2018 with the concerned police authorities for initiating appropriate action for the violations of the FCRA, *inter alia*, alleged

to have been committed by the noticee within the stipulated time as specified under section 29A(2)(e). I also note from the records that on the basis of the said complaint of SEBI, a FIR dated September 28, 2018 was registered with MIDC Police Station, Mumbai and the same, as noted above, is validly subsisting.

42. I note that the present proceedings under the Intermediaries Regulations have been initiated to adjudge whether the noticee satisfies the criteria for '*fit and proper person*' as specified in the Broker Regulations and the Intermediaries Regulations and the said proceedings are independent of the provisions of FCRA. The noticee is obliged 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. I therefore find no merit in the said submission of the noticee.

43. The noticee has also relied upon the decision of the Hon'ble Supreme Court in the case of *SEBI Vs. Rakhi Trading Private Limited*[2] and Hon'ble SAT in the matter of *Kasat Securities Private Limited* to submit that merely because the noticee acted as a broker, it cannot be concluded that the noticee knew about the nature of transactions or it was guilty of negligence or connivance. The said contention of the noticee has to be seen in light of the fact that the '*paired contracts*' have been held to be in violation of the 2007 Exemption Notification by the Hon'ble Supreme Court (as noted above at para 24). Thus, as understood in light of the above observations of the Hon'ble Supreme Court, the nature of the transactions being carried out on the NSEL platform was simply "financing", whereby fixed returns (e.g. 16%) were being given by one party to the other. The same was apparent on a bare perusal of the "*paired contracts*" executed on the NSEL platform. Considering the above, I do not find any merit in the argument of the noticee that it was not aware of the nature of transactions being carried out on the NSEL platform. Therefore, giving go-by to the terms of the 2007 Exemption Notification and attempting to camouflage the nature of the transactions brings into question, the appropriateness and suitability of the continuance of the registration of the *Noticee,* as a broker.

44. The admission of the noticee having traded in the *'paired contracts'* on the NSEL, which was in violation of the conditions of the 2007 Exemption

[2] [2018] 207 CompCas 443 (SC)

Notification and also the provisions of the FCRA, seriously calls into question the integrity, honesty and lack of ethical behaviour on its part. As observed by the Hon'ble Supreme Court (referred *supra*), these contracts were financing transactions which were portrayed as spot contracts in commodities. The argument that the transactions were entered into at the request of the clients for trading in '*paired contracts'* does not absolve a broker of its responsibility to conduct the diligence required to be performed by any reasonable or prudent person.

45. The role of a registered intermediary including a broker demands from it honesty, transparency, fairness and integrity as has been laid down in Clause 3(a) of Schedule II of the Intermediaries Regulations. SEBI under its mandate to protect interest of investors apart from regulations and development of the securities market is empowered to grant registration to various classes of entities including brokers, who have a very important role in ensuring a fair, transparent and efficient market to the investors. Thus, a broker is bound to act in an honest and ethical manner and comply with all applicable regulatory requirements which would be in the best interests of investors. Here, I also deem it appropriate to note that the noticee cannot take the defence of having a legitimate expectation that the NSEL as an exchange was, *per se*, in compliance with the 2007 Exemption Notification. In view of the decisions of the Hon'ble Supreme Court, wherein the Hon'ble Court has observed that NSEL was advertising fixed returns of 16% and offering '*paired contracts*' as an alternate for fixed deposits, I am of the view that the noticee was under statutory obligation to act with due skill, care and diligence in conduct of all its business and thus, it cannot be absolved of its duty to act with such care and skill in the garb of legitimate expectation.

46. In view of the above, I hold that the noticee does not satisfy the '*fit and proper person'* criteria specified in Schedule II of the Intermediaries Regulations and therefore, the continuance of the noticee as a broker will be detrimental to the interest of the securities market. Hence, action as proposed in the SCNs needs to be taken in the interest of the securities market.

47. At this juncture, I also note that necessity of specifying a period of time as stipulated by the SAT Order, after which the applicant may become eligible to seek registration does not arise in this order (unlike in the case of entities desiring to be registered as market intermediaries) while dealing with an entity

holding a certificate of registration which is recommended to be cancelled, as this forum cannot presume whether such entity would wish to reapply to be a market intermediary or not. If it chooses to do so, it will have to be assessed at such point of time if it is fit and proper as per the extant and applicable provisions.

48. Having examined and dealt with all the contentions raised by the noticee in the preceding paragraphs, I concur with the recommendation made by the DA.

ORDER

49. In view of the foregoing discussions and deliberations, I, in exercise of powers conferred upon me under Section 12 (3) and Section 19 of the SEBI Act, 1992 read with regulation 27 of the SEBI (Intermediaries) Regulations, 2008, cancel the Certificate of Registration (bearing No. INZ000022932) of the noticee i.e. Skung Commxperts Limited.

50. The noticee shall, after receipt of this order, immediately inform its existing clients, if any, about the aforesaid direction in paragraph 49 above.

51. Notwithstanding the direction at paragraph 49 above, the noticee shall allow its existing clients, if any to withdraw or transfer their securities or funds held in its custody, within 15 days from the date of this order. In case of failure of any clients to withdraw or transfer their securities or funds within the said 15 days, the noticee shall transfer the funds and securities of such clients to another broker registered with SEBI within a period of next 15 days thereon, under advice to the said clients.

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

53. The above Order is without prejudice to the criminal complaint filed by SEBI in the NSEL matter and/or any proceedings pending before any authority in respect of similar matter involving the noticee.

54. It is clarified that in view of the amendment made w.e.f. January 21, 2021 in the Intermediaries Regulations, 2008, the procedure for action on receipt of recommendation of a DA prescribed under regulation 28 of the Intermediaries Regulations, 2008 has now been incorporated in the amended regulation 27 of the Intermediaries Regulations, 2008. Accordingly, this order is passed under the amended regulation 27 of the Intermediaries Regulations, 2008.

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

Sd/-

DATE: MAY 10, 2023
PLACE: MUMBAI

ANAND R. BAIWAR
EXECUTIVE DIRECTOR
SECURITIES AND EXCHANGE BOARD OF INDIA