

SECURITIES AND EXCHANGE BOARD OF INDIA

FINAL ORDER

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

In respect of:

Name of the Noticee	SEBI Registration No.
Arcadia Commodities and Trading	INZ000048620

In the matter of National Spot Exchange Limited (NSEL)

A. BACKGROUND

1. Arcadia Commodities and Trading (hereinafter referred to as “**ACT**”/ “**Noticee**”) is registered with Securities and Exchange Board of India (hereinafter referred to as “**SEBI**”) as a stock broker bearing registration no. INZ000048620. ACT was earlier a member of National Spot Exchange Limited (hereinafter referred to as the “**NSEL**”).
2. The present proceedings originate from the enquiry report dated December 24, 2019 (hereinafter referred to as the “**Enquiry Report**”), submitted by the Designated Authority (hereinafter referred to as the “**DA**”) in terms of regulation 27 of the SEBI (Intermediaries) Regulations, 2008 (hereinafter be referred to as the “**Intermediaries Regulations**”) as it stood at the relevant point of time prior to its amendment vide SEBI (Intermediaries) (Amendment) Regulations, 2021, w.e.f.

January 21, 2021. The DA, based on findings recorded in the said Enquiry report, recommended that the registration of ACT as a stock broker may be cancelled.

B. SHOW CAUSE NOTICE, REPLY AND HEARING

3. Pursuant to the Enquiry Report, a post enquiry show cause notice dated February 25, 2020 (hereinafter referred to as “**SCN**”) was issued to the Noticee, along with copies of (i) the aforesaid Enquiry Report; (ii) Finance Ministry letter dated December 30, 2014 to Forward Markets Commission (“**FMC**”); (iii) Hon’ble Bombay HC’s order in criminal bail application no. 1263 of 2014 in Jignesh Prakash Shah vs. State of Maharashtra dated August 22, 2014. In response to the SCN, the Noticee filed a reply dated July 30, 2020.
4. While the aforesaid proceedings were pending, SEBI passed five separate orders rejecting the applications filed by five other entities for registration as commodity brokers in NSEL matter during February 2019. Aggrieved by the said SEBI orders, the entities filed separate appeals before the Hon’ble Securities Appellate Tribunal (“**Hon’ble SAT**”). The Hon’ble SAT *vide* its common order in the matter of Geofin Comtrade Ltd. And Ors. vs. SEBI (Appeal no. 214 of 2019) dated June 09, 2022 (“**June 2022 SAT Order**”), remanded the aforesaid SEBI orders to decide these matters afresh within six months from the date of the said order. While remanding the aforesaid SEBI orders, the Hon’ble SAT *inter alia* held as under:

“...

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

5. In light of the June 2022 SAT Order, it was felt necessary to furnish certain additional documents/material to the Noticee and grant an opportunity of personal hearing, before concluding the present proceedings. Accordingly, a supplementary SCN dated February 27, 2023 ("**SSCN**") was served on the Noticee along with the following documents:
 - 5.1. Copy of SEBI complaint dated September 24, 2018 filed with Economic Offences Wing ("**EoW**");
 - 5.2. Copy of FIR dated September 28, 2018 filed by SEBI under section 154 of Criminal Procedure Code, 1973 ("**CrPC**"); and
 - 5.3. Amended Schedule II of Intermediaries Regulations.
6. Vide letter dated June 09, 2023, the Noticee requested for inspection of documents and the same was granted on July 03, 2023. Pursuant to the inspection, vide letter dated July 07, 2023, the Noticee again sought certain documents and in response, vide email dated July 13, 2023, the Noticee was informed that all the relevant documents have already been provided to the Noticee during the inspection. Thereafter, the Noticee submitted another reply vide letter dated September 26, 2023. Subsequently, the Noticee was granted an opportunity of personal hearing on October 17, 2023. On the said date, the Authorised Representative of the Noticee appeared before me through video conferencing and reiterated the submissions made in the Noticee's replies.
7. The submissions filed by the Noticee vide its letters dated July 30, 2020, July 07, 2020 and September 26, 2023 and those made during the personal hearing are summarized hereunder:
 - 7.1. The Noticee was not provided with all the documents sought by it.
 - 7.2. There has been an inordinate delay in initiation of proceedings by SEBI and the SCN was issued after a gap of almost 10 years. The Noticee has relied upon the orders of Hon'ble Securities Appellate Tribunal (SAT) in the matters of Ashok Shivilal Rupani & Anr. Vs. SEBI (Appeal no. 417 of 2018) decided on 22.08.2019, Mr. Rakesh Kathotia vs. SEBI (Appeal no. 07 of 2016) decided on 27.05.2019, Aditi Dalal, HB Stockholdings (Appeal no. 114 of 2012) and

Khandwala Securities and the order of the Hon'ble Supreme Court in the case of State of Gujarat v/s Patel Raghav Natha (AIR 1969 SC 1297).

- 7.3. The Designated Authority did not provide all the documents and did not provide an opportunity of personal hearing before submission of Enquiry report. The Noticee has submitted that the SCN is in gross violation of principles of natural justice and relied on the orders of Hon'ble Supreme Court in the cases of *Canara Bank and Ors. vs. Shri Debasis Das and Ors* and *A.R. Antulay v. R.S. Nayak*.
- 7.4. The Noticee was a trading/ clearing member of Multi Commodity Exchange of India Limited ("**MCX**"), National Commodity & Derivatives Exchange Limited ("**NCDEX**"), Indian Commodity Exchange Limited ("**ICEX**"), Multi Commodity Exchange Clearing Corporation Limited ("**MCXCCL**") and National Commodity Clearing Limited ("**NCCL**") during the relevant time. The Noticee was expelled as a member from MCX, MCXCCL, NCDEX, NCCL and ICEX in 2021.
- 7.5. The Noticee vide its letter dated August 28, 2021 informed SEBI that the Exchanges have expelled it as their member and so the Noticee intends to voluntarily surrender its SEBI registration.
- 7.6. The Noticee has submitted that w.e.f. July 20, 2021, the Noticee is no longer a SEBI registered intermediary as per Regulation 9(a) of SEBI (Stock Brokers) Regulations, 1992 and section 2(g) of SEBI (Intermediaries) Regulation, 2008. Since the Noticee was expelled as a member by the Exchanges and Clearing Corporations, its registration is cancelled.
- 7.7. The Noticee has relied on SEBI orders in the matter of NSEL in respect of Camco Commodities Private Limited, Smart Commodity Brokers Pvt. Ltd., Sharekhan Commodities Pvt. Ltd., Prudent Comder Private Limited, Tradebulls Commodities Broking Private Limited and Mauzampuriah Agros Private Limited.
- 7.8. The Noticee has requested to drop the proceedings since the proceedings get abated on the ground that it ceased to exist as a SEBI registered intermediary w.e.f. July 20, 2021.
- 7.9. The Noticee has submitted it had only two clients who traded in 'paired contracts' and earned only INR 3,600 as brokerage.

C. BRIEF HISTORY OF NSEL SCAM

8. Before moving forward to consider the matter on merits, the background facts necessary for the present proceedings are narrated in brief as under:

8.1. NSEL was incorporated in May 2005 with the purpose of developing an electronic spot exchange for trading in commodities. In exercise of powers conferred under section 27 of the FCRA, the Central Government *vide* the 2007 Exemption Notification, granted an exemption to all forward contracts of one-day duration for the sale and purchase of commodities traded on NSEL from operations of the provisions of the FCRA subject to certain conditions. The said notification *inter alia* stated that “*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*”. 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.

8.2. In October 2008, NSEL commenced operations providing an electronic trading platform to its participants for spot trading of commodities, such as bullion, agricultural produce, metals, etc. It is observed that NSEL had introduced the concept of ‘paired contracts’ in September 2009 which allowed buying and selling in same commodity through two different contracts at two different prices on the exchange platform wherein the investors could buy a short duration contract and sell a long duration contract and *vice versa* at the same time and at a pre-determined price. The trades for the buy contract (T+2 /T+3) and the sell contract (T+25/T+36) used to happen on 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.

8.3. On February 06, 2012, the erstwhile FMC was appointed by DCA 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 measure, if needed, to protect investors' interest.

8.4. DCA on April 27, 2012 directed NSEL to show cause as to why action should not be initiated against it for violation of the conditions mentioned in the 2007 Exemption Notification.

8.5. Subsequent to the above, NSEL filed a reply. Further, MCA sought comments of FMC on the said replies. MCA also sought certain information from NSEL pursuant to which *vide* its letter dated July 12, 2013, MCA directed NSEL to give an undertaking that:

8.5.1. No further/fresh contracts shall be launched by NSEL until further instructions from the concerned authority; and

8.5.2. All the existing contracts will be settled on the due dates

8.6. NSEL issued a circular on July 31, 2013 suspending its spot exchange operations.

8.7. On August 27, 2013, FMC directed a forensic audit of NSEL by Grant Thornton LLP. Further, the Union of India ordered an inspection of accounts of NSEL and 63 Moons Technologies Ltd. (*earlier FTIL*) under section 209A of the Companies Act. The EoW also registered cases against the directors and key management personnel of the NSEL and 63 Moons (*earlier FTIL*) and against trading members and brokers of NSEL under the provisions of the Indian Penal Code and Maharashtra Protection of Interest of Depositors Act, 1999 ("**MPID Act**").

8.8. After analysing the trade data received from NSEL and the forensic audit report submitted by Grant Thornton LLP, the FMC passed Order dated December 17, 2013 in the matter ("**FMC Order**") wherein it *inter alia* observed that Financial Technologies (India) Ltd. is not a fit and proper person to continue to be a shareholder of 2% or more of the paid-up equity capital of MCX. Further, from paragraph 8 of the FMC Order, I note that the DCA *vide* its letter dated April

27, 2012 directed NSEL to explain as to why action should not be initiated against NSEL for violation of the conditions of the 2007 Exemption Notification. 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 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:

8.8.1. 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 the 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*” as stated in the 2007 Exemption Notification.

8.8.2. 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 2007 Exemption Notification does not specify the delivery period, NSEL had to settle the delivery for all open positions 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.

8.9. On September 19, 2014, Ministry of Finance, Government of India, issued a notification withdrawing the exemption granted to NSEL *vide* the 2007 Exemption Notification.

8.10. From the above, it is clear that NSEL had permitted contracts of various commodities having duration longer than 11 days and these contracts were in contravention of the exemption granted to NSEL. Subsequently, certain entities who were primarily borrowing on the NSEL platform through the modus

of trading in the aforesaid “paired contracts” defaulted in fulfilling their payment obligations leading to a huge settlement default of outstanding contracts to the tune of Rs. 5600 Crores.

8.11. EoW, Mumbai, vide letter dated April 04, 2015, had forwarded an interim report in connection with the investigation conducted by them to identify the role played by the broking houses in the NSEL case. The relevant extracts of the said interim report are as follows:

“IV. Objectives of this investigation into the brokers’ role: A scam of this magnitude would be difficult to continuously occur for 3 years without some of the large brokers’ gross negligence or perhaps active participation.

The actual role of the brokers was:

- To bring in investors to invest in ‘pair trades’ promising them assured returns and the investors got about 13-16% p.a. for investing in the commodity*
- The sellers got finance at 18-20 or more % by pledging their commodity in NSEL warehouses*

They got brokerage from investors on the NSEL platform, and those brokers who had their NBFCs got additional revenue by financing investors for investing on NSEL.

Though the matter is still under investigation, brokers have also received back from exchange certain charges collected from investors such as transaction fees, delivery and warehousing charges, etc. It is suspected that these are indirect motivation incentives for brokers to generate huge volumes. It is also possible that brokers may have benefitted from or compensated by the sellers or defaulters.

The higher the trading turnover, the higher revenues for the exchange and the brokers. Therefore, both wanted to increase turnover at the exchange.

In light of the foregoing, the objective of EOW in investigating brokers was to inquire whether they had been involved in any wrongdoing connected with trading on NSEL, specifically, to determine whether they participated in

a) Any activities which were detrimental to the investors, NSEL, or third parties. To determine whether they had made false and misleading representations, offered inducement, financing and deliberately made wrongful assertions purely to get brokerage and facilitate NSEL in generating higher volumes.

b) Whether they had any illegitimate personal enrichment, or, there has been knowing dereliction in their duties as clearing and forwarding agents towards the commodities and protect the investors.

c) It was also deemed necessary to ensure that their activities were within the framework of law.

8.12. Vide the Finance Act, 2015, FMC was merged with SEBI on September 28, 2015 in pursuance thereof SEBI was entrusted with the powers to regulate the trading in commodities futures market. As per the said act, an existing intermediary could continue to buy, sell or deal in commodity derivatives as a commodity broker, if it would make an application for its registration as an intermediary to SEBI within a period of 3 months from the date of merger till the disposal of such application by SEBI. Accordingly, the Noticee on the basis of an application so made by it, was granted SEBI registration number to operate as a stock broker in the securities market. In terms of the said act, FCRA was also repealed with effect from the aforesaid date.

8.13. On September 24, 2018, SEBI filed a complaint with EoW to initiate appropriate action against brokers/members of NSEL and other persons in the NSEL matter under sections 20, 21 and other appropriate provisions of the FCRA.

8.14. On September 28, 2018, SEBI gave a statement to the police which resulted into a FIR under section 154 of CrPC.

8.15. It is also pertinent to refer to the judgment of the Hon'ble Supreme Court decided on April 30, 2019, passed in the matter of 63 Moons Technologies Ltd. (formerly known as Financial Technologies India Ltd.) & Ors. vs. Union of India & Ors. (Civil Appeal No. 4476 of 2019) (2019)18 SCC 401 ("**Merger Petition**"), 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....."

8.16. Further, in 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) ("**MPID matter**"), the Hon'ble Supreme Court while drawing reference to the presentations made by 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."

8.17. In the background of the aforesaid discussion pertaining to “paired contracts” as captured in the preceding paragraphs, I now move on to examine whether the Noticee satisfies the “fit and proper person” criteria as laid down in Schedule II of the Intermediaries Regulations.

D. CONSIDERATION OF ISSUES AND FINDINGS

9. I find it appropriate to first deal with the preliminary contentions raised by the Noticee.

10. The Noticee has argued that there has been an inordinate delay in initiation of present proceedings and that the SCN was issued after a gap of almost 10 years. In support of the same, the Noticee has relied upon the cases of *Ashok Shrivastava & Anr. Vs. SEBI (supra)*, *Mr. Rakesh Kathotia vs. SEBI (supra)*, *Aditi Dalal (supra)*, *HB Stockholdings (supra)*, *Khandwala Securities (supra)* and *State of Gujarat v/s Patel Raghav Natha (supra)*.

11. In this regard, I note that the NSEL scam unfolded in 2013 after which several agencies such as EoW, SFIO, etc. conducted investigations into the activities of NSEL. Further, FMC, Hon'ble Bombay HC and Hon'ble SC made important pronouncements relating to different facets of the matter such as whether merger of NSEL with FTIL should be permitted and whether NSEL can be considered as a “financial establishment” under the MPID Act. A large number of brokers had allegedly participated in the illegal contracts at NSEL platform. After the merger of FMC with SEBI on September 28, 2015, some of these brokers applied for registration with SEBI. Thereafter, assessing all the factual circumstances available before SEBI and considering the importance of fulfilling “fit and proper person” criteria by brokers, action was duly initiated against the set of brokers who executed the alleged trades. Thus, in absence of any prejudice caused to the Noticee, merely because proceedings were initiated in 2018 by way of DA SCN, I find that the present proceedings do not stand vitiated. Further, I note that after issuance of DA SCN, June 2022 SAT Order was passed by Hon'ble SAT wherein it set aside the impugned orders of WTM concerning similar facts and evidence as

the present case. I find it appropriate here to briefly delve into the grounds on which the impugned orders of SEBI were set aside by Hon'ble SAT leading to the issuance of SSCN. The grounds are as follows:

- (i) The observations of the Hon'ble Bombay High Court in the matter of 63 Moons vs. Union of India (Writ Petition No. 2743 of 2014 dated December 04, 2017) cannot be relied upon as the said judgement has been set aside in appeal by the Hon'ble Supreme Court in the Merger Petition judgment.
- (ii) The observation from the order dismissing the Writ Petition filed by NSEL against the invocation of the MPID Act in NSEL vs. State of Maharashtra and Ors. (Writ Petition No. 1403 of 2015 dated October 01, 2015), cannot be relied upon, as in a subsequent Writ Petition moved by 63 Moons Technologies Ltd., in Writ Petition No. 1181 of 2018, a Division Bench of the Hon'ble Bombay High Court observed that the *prima facie* observations made in its earlier order were not binding and the same was observed since further investigation was in process at the relevant stage.
- (iii) The observations in the bail rejection order dated August 22, 2014, passed by the Hon'ble Bombay High Court in the matter of Jignesh Prakash Shah vs. The State of Maharashtra, cannot also be relied upon as such observations were limited to the fact as to whether the bail should be granted or not.
- (iv) Reliance on the SFIO Report was misplaced. The report only directs EoW/Police to initiate appropriate proceedings against NSEL and its directors/promoters. Based on the SFIO Report, the Special Sessions Judge took cognizance of the matter by an order dated July 29, 2019 which was challenged due to jurisdiction before Hon'ble Bombay High Court. The Hon'ble Bombay High Court by an order dated January 15, 2020 passed an interim order staying the effect and operation of the impugned order dated July 29, 2019.

- (v) Reliance placed on decisions of the Hon'ble Tribunal in the matter of Jermyn Capital vs. SEBI and Mukesh Babu Securities vs. SEBI is misplaced as decisions in the said matters are distinguishable on facts. Jermyn Capital was held to be in relation to an Interim Order passed by SEBI, and the Hon'ble Tribunal was of the view that the criteria for passing an ad interim order are based on a different criterion, namely *prima facie* case, the balance of convenience and irreparable injury which are distinct and different while considering an application for grant of certificate of registration. The decision in the matter of Mukesh Babu Securities was distinguished by the Hon'ble Tribunal on the basis that in the said matter a criminal complaint was filed against the chairman of the company. The Hon'ble Tribunal noted that with respect to the appellants, there is no evidence to show that any proceedings have yet been initiated against the appellants in the matter under consideration.
- (vi) Regarding close association of the appellant with NSEL, forensic report which was made at the behest of SEBI has exonerated the appellant on this charge. This fact has not been considered by the WTM while holding the appellant to be closely connected with NSEL. There is no finding in the impugned cases indicating that the appellants have any control directly or indirectly over NSEL and, therefore, the question as to whether the appellant is a close associate of NSEL has not been considered in the right perspective.
- (vii) In the impugned cases, the application for grant of registration certificate has been rejected without specifying how long the rejection of application would continue. Such rejection cannot continue indefinitely and if an application is rejected, a period should be prescribed within which the broker cannot apply for grant of a fresh registration certificate but after the expiry of the period he could file such an application.

12. The SSCN issued pursuant to the June 2022 SAT Order takes into consideration additional material available on record. The issuance of SSCN, delivery of SSCN, examining the reply to the SSCN and hearing conducted thereafter, were essential steps in ensuring that principles of natural justice are being met at the cost of prolonging the conclusion of present proceedings. Therefore, I find that the events detailed above necessitated an extended period for concluding the proceedings.
13. The Noticee has also contended that all the documents sought by the Noticee was not provided to it. I note that Sub-regulations (3) and (4) of Regulation 25 of the Intermediaries Regulations specify that the copies of the documents “relied upon by SEBI” along with the extracts of relevant portions of the reports containing the findings arrived at in an inquiry, investigation or inspection, if any, shall be provided to the Noticee. On perusal of paragraph 9 and 10 of the Enquiry Report, I note that the Noticee was provided with the following documents relied upon by SEBI in the present proceedings:
- 13.1. Copy of the relevant FMC Order with Annexures;
 - 13.2. Copy of the Grant Thornton Report with Annexures;
 - 13.3. Copy of the Notification issued by the Ministry of Consumer Affairs dated June 05, 2007;
 - 13.4. Documents explaining specifications of ‘paired contracts’ (as available in the Grant Thornton Report) (which is narrated in the FMC order);
 - 13.5. List of trading members/ fund name and clearing member name and the amount mentioned against their name in the EOW interim report dated April 04, 2015, who have applied/ registered with SEBI (the amount indicates default amount of clients (investors) who traded through the said brokers);
 - 13.6. Copies (total 11) of fortnightly reports submitted by NSEL to the erstwhile FMC;
 - 13.7. List of 148 members against whom NSEL has pay-out obligations as on September 19, 2013 as mentioned in the Grant Thornton Report (as per Annexure 6 of the Grant Thornton Report) dated September 21, 2013; and
 - 13.8. Data containing registration documents of 299 members and Annual Return documents of 234 members.

14. I also note that vide post Enquiry SCN dated February 25, 2020, Noticee was provided with additional material such as letter dated December 30, 2014 of DEA, Ministry of Finance and Order dated August 22, 2014 of the Hon'ble High Court of Bombay in the criminal bail application of *Jignesh Prakash Shah vs. State of Maharashtra*. I further note that vide SSCN dated February 27, 2023, the Noticee was provided with copies of SEBI complaint dated September 24, 2018 filed with EOW and FIR dated September 28, 2018 filed by SEBI. Thereafter, during the inspection of documents on July 03, 2023, the Noticee was provided with copies of NSEL complaint letters dated March 17, 2015 and March 24, 2015, Email dated August 31, 2018 sent by SIT EOW to SEBI, FMC complaint letter dated January 16, 2015 against NSEL and SEBI letter dated July 09, 2018 to EOW. Therefore, I find that all the material / relevant documents have been duly provided to the Noticee in compliance with the principles of natural justice in conducting present enquiry proceedings. Hence, the contention of the Noticee's devoid any merit.

15. The Noticee has also contended that it was not provided with personal hearing before the DA. In this regard, I note that the DA had issued the show cause notice dated September 25, 2018 under the then existing Regulation 25(1) of the Intermediaries Regulations. Thereafter the Enquiry Report was submitted on December 24, 2019. The Intermediaries Regulations were amended vide the SEBI (Intermediaries) (Amendment) Regulations, 2021, w.e.f. January 21, 2021. The amended Regulations now provide that the DA shall grant an opportunity of personal hearing and issue or cause to issue a notice scheduling a date for hearing. Thus, under the then existing Intermediaries Regulations prior to its amendment w.e.f. January 21, 2021, there was no legal requirement for providing the opportunity of personal hearing to the Noticee by the DA as contended by the Noticee. The Regulations specified granting of opportunity of personal hearing by the competent authority, which as has been detailed in the previous paras has been more than adequately provided to and availed by the Noticee. Thus, every opportunity was provided to the Noticee and no prejudice has been caused to the Noticee and there is no defect in the process followed in the present enquiry

proceedings. Accordingly, the contention raised by the Noticee in this regard is also misplaced and devoid of any merit.

16. Before moving forward to examine charges and the evidence available on record, it would be appropriate to take a look at the legal provisions of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as “**SEBI Act**”), which are relevant in the present case. It is alleged that the Noticee has violated (i) regulation 5(e) of SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992 (hereinafter referred to as “**Stock Brokers Regulations**”) read with Schedule II of Intermediaries Regulations; and (ii) regulation 9(b), 9(f) read with clause A (1), A (2) and A (5) of Schedule II of Stock Brokers Regulations. The same are reproduced below for reference:

SEBI Act

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

12. (3) The Board may, by order, suspend or cancel a certificate of registration in such manner as may be determined by regulations: Provided that no order under this sub-section shall be made unless the person concerned has been given a reasonable opportunity of being heard.

Stock Brokers 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; and

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

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

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

SCHEDULE II

Code of Conduct for Stock Brokers

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.

Intermediaries Regulations

Schedule II

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.

17. I note that the Noticee has contended that it had only two clients and that it earned a brokerage of only INR 3,600. On perusal of the Enquiry Report, it is noted that as per the Grant Thornton report, NSEL had a pay-out obligation of INR 8,74,896/- towards the Noticee and as per the interim EOW Report, the Noticee had money exposure to the tune of INR 9,62,450. It is also observed from the Enquiry Report and the NSEL circular dated March 10, 2015 that NSEL had made a special pay-out amounting to INR 4,72,268/- to the Noticee. Further, I find it relevant to refer to the finding of Hon'ble SC in Merger Petition, wherein it *inter alia* held that:

“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.....”

Thus, it is clear that on NSEL (other than E-series contracts) the proportion of paired contracts as a percentage of total trades amounted to 99% in 2013. It is not the Noticee's case that the transactions facilitated by it for its clients were E-series contracts. Accordingly, by inference, transactions on NSEL facilitated by the Noticee, could not have been anything but “paired contracts”.

18. Having established that the Noticee has traded in ‘paired contracts’ on behalf of its clients, I now proceed to examine the allegations levelled against the Noticee in the SCN and the SSCN. It is noted that the main allegation against the Noticee, as levelled in the SCN, is that by facilitating the trading in ‘paired contracts’ on NSEL platform during the relevant period as a Trading Member/ Clearing Member, the Noticee has, *prima facie*, violated the conditions stipulated in the 2007 Exemption Notification and consequently also the provisions of the FCRA. Therefore, it was alleged in the SCN that the continuance of the registration of the Noticee as a broker is detrimental to the interest of the Securities Market and the Noticee is no longer a ‘fit and proper person’ for holding the certificate of registration as a broker in the Securities Market, which is one of the conditions for continuance of registration as specified in regulation 5(e) of the Stock Brokers Regulations read with Schedule II of the Intermediaries Regulations as

applicable at the relevant time. Subsequently, SEBI, on the strength of certain documents/material (such as SEBI Complaint dated September 24, 2018 and FIR dated September 28, 2018 etc.) as provided to the Noticee vide SSCN dated February 27, 2023, further alleged that in light of the aforesaid documents filed against the Noticee by SEBI as well as observations/ findings against the Noticee in the Enquiry Report dated December 24, 2019, the Noticee is no longer a 'fit and proper person' for holding the Certificate of Registration being in violation of regulation 5(e) of the Stock Brokers Regulations read with Schedule II of the Intermediaries Regulations.

19. I note that under the FCRA, a "forward contract" is defined as a "contract for delivery of goods and which is not a ready delivery contract". A 'ready delivery contract' is defined as "a contract which provides for the delivery of goods and the payment of a price therefor, either immediately or within such period not exceeding eleven days". Given these definitions in the FCRA, all the contracts traded on the NSEL which provided for a settlement schedule exceeding 11 days were treated by the FMC as Non-Transferable Specific Delivery Contracts. It is, therefore, seen that while the Ministry of Consumer Affairs (MCA) had stipulated in the Exemption Notification that only forward contracts of 'one-day' were permitted to be offered on the NSEL, the FMC, in its order, relying on the definition of the "forward contract" under FCRA held that the NSEL was allowed to only trade in forward contracts of 'one-day duration' and was obligated to ensure delivery and settlement within 11 days. Thus, 55 contracts of various commodities, having duration longer than 11 days that were executed on the NSEL were paired contracts without regulatory approval and in contravention of the exemption granted to NSEL and thus clearly not in accordance with law.

20. In the merger petition (*63 Moons Technologies Ltd. vs. UOI*), the Hon'ble Supreme Court held that these contracts were in the nature of financing transactions. In the MPID matter (*The State of Maharashtra vs. 63 Moons Technologies Ltd.*), the Hon'ble Supreme Court enlarged the interpretation and held that such transactions come within the definition of 'deposits' under the MPID Act. While extensively referring to the claims made on the website of the NSEL and the contents of the

publicity material and other investor resources, the Hon'ble Court also observed that the NSEL were advertising assured and uniform returns of 16% per annum for the 'paired contracts' traded on the NSEL platform where the return offered was the same across the commodities and that the return remained the same irrespective of the duration of the contract. At paragraph 45 of the said order, the Hon'ble Supreme Court also depicted certain examples of 'paired contracts', which offered assured returns. For example, a T+2 and T+25 paired contract in Steel had the same offered rate of return as a T+5 and T+35 paired contract in Castor Oil. Thus, the judgement of the Hon'ble Supreme Court in the MPID matter highlighted how the 'paired contracts' were being marketed as an alternative to fixed deposits wherein the overwhelming majority of the sale leg of the 'paired contracts' which were executed were in fact short sales and further that, the commodities to back such sales were not available at the designated warehouses of the NSEL.

21. I also note that the scope of the present proceeding is to analyse the apparent impact as well as the consequences of the conduct of the Noticee as per the justification and contentions advanced and also to examine as to whether or not, the Noticee acted in a manner expected of a registered market intermediary. It cannot be denied that the involvement of the Noticee in trading in 'paired contracts' was neither permitted by the Exemption Notification nor by any of the applicable provisions of the FCRA. Under these circumstances, any 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.

22. Despite the above and the discussion in the context of the facts of the case, I have examined at length the other submissions made by the Noticee and also examined whether while transacting in paired contracts, the Noticee could have been under the *bonafide* belief that such transactions were actually spot contracts in commodities or alternatively that since 'paired contracts' were offered, that meant that NSEL was offering contracts which were not resulting in compulsory delivery.

23. In the undeniable background that there was a settlement default at NSEL, it is clear that there were enough red flags which should have alerted the Noticee when these products were first offered by NSEL. With the material on record, it is further clear that any prudent person (including the Noticee) would have come to the conclusion that what was being offered were not spot contracts in commodities and rather had trappings of a financial product which offered fixed and assured returns, as has been already observed by the Hon'ble Supreme Court in the State of Maharashtra vs. 63 Moons Technologies Ltd. The Noticee was expected to do due diligence on the products which it offered for trading to its clients. An assumption as to the legality of 'paired contracts' clearly shows that the Noticee failed to do adequate due diligence. The Notification regarding approval of contracts permitted on NSEL was in public domain. Thus, I find that Noticee failed to perform basic due diligence of the contracts offered *vis-à-vis* the conditions specified in the aforesaid Notification. For these reasons, the Noticee is found to have violated Clause A (1), A (2) and A (5) Code of Conduct of Stock Brokers Regulations.

24. It is a settled position of law that every registered intermediary in the securities market is required to fulfil all the conditions of its registration at all points of its functioning including any additional criteria statutorily provided for, from time to time. Else, there would arise an anomalous situation where an entity that has obtained a certificate of registration after fulfilling the said criteria would fail the test after a period of time and yet continue to function in the securities market despite not fulfilling the required criteria.

25. On this premise, it can be said that the requirement of being a 'fit and proper' person, is a continuing 'eligibility criteria'/ statutory requirement, which ought to be satisfied by all registered entities at all points of time. This condition is not a one-time condition applicable only at the time of seeking registration. Rather, the provisions governing the grant of registration provides that this is a condition which every registered intermediary is required to fulfil, on a continuous basis as long as the entity remains associated with the securities market as a registered

intermediary. Therefore, the criteria of 'fit and proper person', is an ongoing requirement throughout the period during which an entity remains operational in the securities market as a registered intermediary and for this reason, the principles of estoppel do not apply to the instant case of the Noticee. If the continued applicability of the fit and proper criteria to its functioning is challenged, there would exist a market where the overall interest of the investors would stand compromised.

26. 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 and Regulation 9(b) of the Stock Brokers Regulations mandates a registered stock broker to abide by the rules, regulations and bye-laws of the stock exchange which are applicable to it. In terms of Regulation 9(f) of the Stock Brokers Regulations, a registered stock broker is required to abide by the Code of Conduct as specified in Schedule II of the Stock Brokers Regulations. I further note that the 'fit and proper person' criteria specified in Schedule II of the SEBI (Intermediaries) Regulations, 2008, was amended vide SEBI (Intermediaries) (Third Amendment) Regulations, 2021 with effect from November 17, 2021.

27. Thus, as and when any of the 'fit and proper' criteria change, every registered entity is required to comply with the revised criteria, including as in this instance, the criteria as revised vide the amendment in November 2021. The requirement is not a onetime condition applicable only at the time of seeking registration. Rather, the provisions governing the criteria provides it to be a condition which each and every registered intermediary is required to fulfil on a continuous basis as long as the entity remains associated with the securities market as a registered intermediary. 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 at any point of time.

28. The parameters provided under paragraph 3(b) of the amended criteria of Schedule II of the Intermediaries Regulations lay down a list of disqualifications which, *inter alia*, include the following:

“(1).....

(2).....

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

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

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

.....”

29. As detailed in the SSCN, FIR was registered by the EOW with the MIDC Police Station, Mumbai, against the Noticee under section 154 of the CrPC on September 28, 2018. This has not been challenged, quashed or stayed by any competent court *qua* the Noticee till date. The disqualifications listed under paragraph 3(b) of the amended criteria of Schedule II of the Intermediaries Regulations are unambiguously clear and no exemption from such criteria has been provided. Once the disqualification is triggered, the ‘fit and proper’ person criteria is open for determination by SEBI. The disqualification provided in paragraph 3(b)(i) under the amended Schedule II of the Intermediaries Regulations has also been triggered *vis-à-vis* the Noticee.

30. Thus, by virtue of its conduct, trades and being a member of NSEL, the Noticee acted as an instrument in promoting and/or dealing in ‘paired contracts’ which were in the nature of financing transactions (as held by the Hon’ble Supreme Court of India referred *supra*). By providing a platform for trading to its clients and by providing access for taking exposure to such ‘paired contracts’, the Noticee exposed its clients to the risks involved in trading in a product that did not have regulatory approval.

31. Further, the Noticee has also attracted disqualification under Clause 3(b)(i) of the amended provisions of Schedule II of the Intermediaries Regulations on account of this complaint filed by SEBI and the FIR that was registered by the EOW based on the said complaint of SEBI, and the complaint remains pending.

32. In view of the above, I note that the Noticee has traded in “paired contracts” on behalf of its clients on NSEL. The execution of such paired contracts shows participation of the Noticee in the said scam which raises questions regarding the integrity, honesty, ethical behaviour, reputation, fairness and character of the Noticee. The Noticee has also attracted disqualification under clause 3(b)(i) under the amended Schedule II of the Intermediaries Regulations which states that pendency of a criminal complaint filed is a ground that SEBI may take into consideration for determining whether any person is a “fit and proper person”.
33. The facts and circumstances along with other material available on record clearly leads me to the conclusion that the Noticee has not satisfied the “fit and proper person” criteria specified in Schedule II of the Intermediaries Regulations.
34. The Noticee has also submitted that with effect from July 2021, the Noticee was expelled from the membership of MCX, NCDEX and ICEX. Regulation 9(a) of the Stock Brokers Regulations provides that any registration granted by SEBI is subject to the condition that the stock broker holds the membership of any stock exchange. I have perused the copies of the circulars of the Exchanges for expulsion of membership submitted by the Noticee and I have also verified the said circulars from the websites of the Exchanges¹. As per regulation 27(i) of Stock Brokers Regulations, ceasing to be a member of a stock exchange is one of the grounds for suspension or cancellation of registration as a stock broker.
35. In view of the above, I am inclined to accept the recommendation made in the Enquiry Report that the certificate of registration granted to the Noticee should be cancelled.

¹https://ncdex.com/public/uploads/circulars/3%20Expulsion%20circularr_Arcadia%20Commodities%20&%20Trading_1626695290.pdf
https://www.icexindia.com/docs/default-source/circulars/circular_expulsion-of-arcadia-commodities-trading.pdf?sfvrsn=975dcb8d_6
https://www.mcxindia.com/docs/default-source/circulars/english/2021/july/circular-437-2021.pdf?sfvrsn=aab45391_0

E. ORDER

36. In view of the facts and circumstances of the case and the conclusions arrived at discussed above, I, in exercise of powers conferred upon me under Section 12(3) and Section 19 of the SEBI Act read with regulation 27 of the Intermediaries Regulations, hereby cancel the certificate of registration (bearing registration no. INZ000048620) of the Noticee i.e. Arcadia Commodities and Trading.

37. The Order shall come into force with immediate effect.

38. This Order is without prejudice to the criminal complaint filed by SEBI in the NSEL matter and/ or any proceedings pending before any authority in respect of similar matter concerning the Noticee or other relevant persons.

39. A copy of this Order shall be served upon the Noticee and upon all recognized stock exchanges and depositories.

Sd/-

ANANTH NARAYAN G.

DATE: OCTOBER 23, 2023

WHOLE TIME MEMBER

PLACE: MUMBAI

SECURITIES AND EXCHANGE BOARD OF INDIA