

Commodity
Market-
Status on
Merger of
FMC with
SEBI



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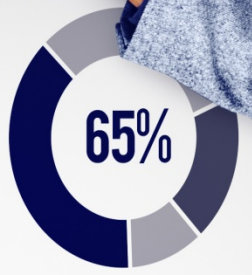
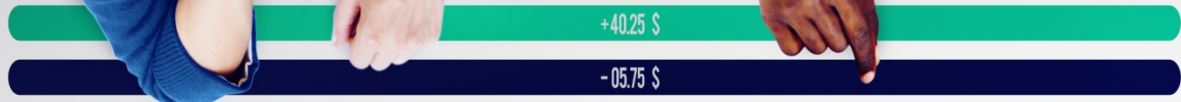
PRESENCE IN INDIA

- Gandhinagar
- Kolkata
- Dhanbad
- Bengaluru
- Delhi
- Mumbai
- Varanasi
- Assam
- Rudrapur
- Siliguri
- Raniganj

OVERSEAS PRESENCE

- Dubai
- Belgium
- Hong Kong
- Mauritius
- Moscow





LSM/VK	EJ+EO	IDGH	EJ+EO	LSM/VK	EJ+EO	EJ+EO	IDGH	EJ+EO	EJ+EO	IDGH	EJ+EO
▲ 24.7050	▲ 86.560	0.650	86.560	▲ 24.7050	▲ 86.560	86.560	0.650	86.560	▲ 86.560	0.650	86.560
▲ 47.0540	▲ 57.030	807.5	57.030	▲ 47.0540	▲ 57.030	57.030	807.5	57.030	▲ 57.030	807.5	57.030
▲ 6760.70	▲ 5.7540	0.607	5.7540	▲ 6760.70	▲ 5.7540	5.7540	0.607	5.7540	▲ 5.7540	0.607	5.7540
▲ 24.7050		0.650	86.560	▲ 24.7050		86.560	0.650	86.560			



▲ 24.7050	▲ 86.560	0.650
▲ 47.0540	▲ 57.030	807.5
▲ 6760.70	▲ 5.7540	0.607





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Commodity Market



- Commodity market is an important constituent of the financial markets of any country. It is the market where a wide range of products, viz., precious metals, base metals, crude oil, energy and soft commodities like palm oil, coffee etc. are traded. It is important to develop a vibrant, active and liquid commodity market. This would help investors hedge their commodity risk, take speculative positions in commodities and exploit arbitrage opportunities in the market.
- Commodity Market is regulated by Forward Market Commission (FMC)
- In the Union budget for 2015-16, Union Finance Minister proposed merger of Forward Market Commission with SEBI.
- The commodity derivatives exchanges shall be deemed recognized stock exchanges under SCRA,1956 and thus all provisions for recognized stock exchanges would ultimately apply to them.
- For merger, Finance Act 2015 provided for amending the SCRA,1956 and FCRA, 1952.

Commodity Exchanges



Currently there are 12 recognised associations under FCRA

- ◉ 6 National Commodity Exchanges(NMCEs), out of 6 only 3 are operational. They are:
 1. MCX
 2. NCDEX
 3. NMCEX
- ◉ 6 Regional Commodity Exchanges(RMCEs), out of 6 only 3 are operational. They are:
 1. The Chamber of Commerce, Hapur
 2. India Pepper & Spice Trade Association, Kochi
 3. Rajkot Commodity Exchange Ltd.

Commodity Exchanges



FMC vide circular dated May 19,2015, has issued directions to non-Operational Exchanges. They are:

- Refund of client money within 15 days
- Resolving client disputes within 6 months
- Refund of member deposits

An analysis of the present status of commodity derivative exchanges with the requirement of SCRA was carried out. And following findings and solutions are made in the form of:

- Gaps
- Proposals

respectively

Corporatization And Demutualization



Gap

- As per section 4A of SCRA 1956, All recognized to be corporatized and demutualised
- FMC required National commodity derivative exchanges to be corporatized and demutualised, However there is no such requirement for regional commodity derivative exchanges.

Proposals (Issuance of Circulars)

1. SEBI to issue circular specifying mandatory conditions for minimum turnover, infrastructure etc. National Exchanges may be required to meet the prescribed conditions within 2 years from the date of merger
2. Regional exchanges maybe required to corporatize and demutualise within a period of 3 years from the date of merger

Clearing & Settlement Rights



Gap

- Regulation 2(e) of SECC 2012 defines clearing member as a person having clearing & settlement rights in an recognised clearing corporation
- Commodity exchanges clear & settle their own clearing house, person having clearing & settlement right are members of such exchanges itself

Proposals (Amendment to Regulation 2(e) of SECC 2012)

1. The definition of clearing members be modified to include persons having clearing and settlement rights in a commodity derivative exchange
2. It is proposed to define 1. Commodity Derivative exchange 2. National derivative exchange 3. Regional commodity derivatives exchange in SECC Regulations.

Recognition of Stock Exchanges Clearing Corporations



Gap

- Regulation 3 of Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 (SECC) prohibits persons from organizing stock exchange or clearing corporation unless recognition is obtained from SEBI
- Regulation 4 to 13 cover procedure for new recognition, eligibility criteria, regulatory fee and withdrawal of recognition
- Regulation 12(5) requires recognized stock exchanges to comply with the conditions of recognition as given in regulations 7(2) and 7(3) on a continuous basis and recognized clearing corporation to comply with the conditions of recognition as given in Regulations 7(2) and 7(3)

Recognition of Stock Exchanges and Clearing Corporations



Gap

- Commodity derivative exchanges
 1. Clear and settle through their own clearing house.
 2. Under FCRA, there is no requirement to transfer the functions of clearing & settlement to a clearing corporation.
 3. They do not provide novation or act as a central counter party to the transactions executed on the exchange platform.
 4. As per Submissions made by commodity derivative exchanges, this limitation is because of complex taxation matters, issues relating to mandi registrations, licenses, control orders, invoicing denoting ownership of the commodities, physical location of the commodities and its movement applicable to transactions in commodities

Recognition of Stock Exchanges and Clearing Corporations



Gap

- The recognition under Commodity derivative exchanges under FCRA is permanent for all the national and regional commodity derivative exchanges except for 2 regional exchanges. They are:
 1. The Chamber of Commerce, Hapur – Recognition granted up to February 28,2018
 2. Rajkot Commodity Exchange Ltd.- Recognition granted up to March 31,2018

Proposals(Issuance of circular)

1. The validity of recognition of deemed recognized stock exchanges may be taken to be same as the validity of their current recognition under FCRA

Recognition of Stock Exchanges and Clearing Corporations



Proposals (Issuance of circular)

2. The conditions given in regulation 7(2) (i.e. Compliance with ownership, governance and net worth norms, demutualisation, corporatization, directors, shareholders etc) may be made applicable to commodity derivative exchanges
3. The conditions given in regulation 7(3) (i.e. Online screen based trading system, online surveillance capability, adequate investor protection fund and investor services fund, facility for real time dissemination of trade information, BCP, DRS etc) & regulation 7(4) (i.e. Necessary infrastructure for timely clearing & settlement, risk management mechanism, wide network of clearing members etc. may be made applicable to NCDE within 1 year and to RCDE within 3 years from the date of the merger

Recognition of Stock Exchanges and Clearing Corporations



Proposals (Issuance of circular)

4. CDE may be required to comply with the requirement of availing services of clearing corporation for clearing & settlement of trades within 3 years from the date of merger. Till then it is proposed to allow them with their present arrangement.
5. The conditions complied given in regulation 7(4) may be made applicable. However, CDE may be required to continue providing guarantee for settlement of trades including good delivery
6. Regulation 11 (Regulatory Fee. Minimum fee INR 1,00,000) and Regulation 13 (Withdrawal of recognition) may be made applicable to CDE from the date of merger except that RCDE be levied at flat fee of INR 50,000 per annum for the first 2 years post-merger

Net Worth

Gap

- Regulation 14 prescribes
 1. Net worth requirement (INR 100 crores) for stock exchanges
 2. Prohibits distribution of dividends till prescribed net worth is achieved
 3. Requires submission of audited net worth certificate to SEBI on a yearly basis

- FMC vide its circular dated May 06,2014 prescribes
 1. Net worth requirement and its definition in NCDE is in line with SCEE Regulations 2012, However, there is no specific net worth requirement prescribed for RCDE

Net Worth of CDE as on 31st March 2015

S.No	Name of the Exchange (NCDE)	Net Worth (In INR Crore)
1	MCX	845.7
2	NCDEX	287.4
3	NMCEX	58.43
4	Ace Derivatives and Commodity Exchange Limited, Mumbai	17.12
5	India Commodity Exchange Limited, New Delhi	1
6	Universal Commodity Exchange Ltd, Navi Mumbai	23.32

As per FMC vide circular dated May 06, 2014, NCDE having net worth less than INR 100 crores have time till May 05, 2017

Net Worth

Proposals

- For NCDE, Time line granted by FMC till May 05,2017 of minimum net worth of INR 100 crores may be retained
- For RCDE, time line is 3 years from the date of merger
- Further, in terms of Regulation 14(4), CDE may be prohibited from distributing profits till net worth is achieved.

Ownership

Gap

- Regulation 15 to 22 pertain to shareholding norms including disclosure of shareholding to SEBI and record keeping of shareholding details
- SECC Regulations 2012 permit following five categories of persons to hold up to 15% of shares of stock exchanges (i) a stock exchange (ii) a depository (iii) a banking company (iv) an insurance company (v) a public financial institution.
- SEBI has prescribed the format for reporting shareholding of stock exchanges on a qtrly basis

Ownership

Gap

- FMC vide its circular dated May 06,2014 prescribes shareholding norms of NCDE is in line with SCEE Regulations 2012, However, FMC has not prescribed shareholding norms for RCDE
- FMC has allowed the following persons to hold up to 15% in NCDE (i) a commodity exchange (ii) a stock exchange (iii) a depository; (iv) a banking company (v) an insurance company (vi) a public financial institution. Out of 6 NCDE, only MCX is complaint with the shareholding requirements. However FMC vide circular dated May 06,2014 has given time till May 5,2019 to comply with the same.
- FMC has not specified any format for the shareholding pattern

Ownership

Proposals

- The SECC requirements may be made applicable to NCDE from the date of merger for processing the applications for approval of holding shares in CDE. However, the holdings of existing shareholders already approved by FMC need not be approved by SEBI.
- NCDE may be required to submit shareholding pattern in the format prescribed by SEBI on a quarterly basis
- The timeline granted by FMC to NCDE till May 05,2019 to comply with ownership norms may be retained
- Regarding RCDE, the time line co-terminus with that provided for corporatization and demutualization may be allowed to comply with ownership norms

Governing Boards and Directors



Gap

- Regulations 23 to 26 prescribe governing board to include Public Interest Directors, Shareholder Directors and Managing Directors
- SEBI has defined Public Interest Director, Shareholder Director and Associates
 1. Public Interest Directors- An Independent director, representing the interests of investors in securities market and who is not having any association, directly or indirectly
 2. Shareholder Directors- a director who represents the interest of shareholders, and elected or nominated by such shareholders who are not trading members or clearing members, as the case may be, or their associates and agents;

Governing Boards and Directors



Gap

- For appointment of Chairperson, SECC Regulation 2012 state that subject to prior approval of the Board, the chairman shall be elected by governing board.
- At least one public interest director shall be present in the meeting of the governing board to constitute the quorum
- As per SEBI norms, Public interest directors shall be nominated for a fixed term of three years, or for such extended period, as may be approved by the Board
- SECC Requirements do not allow representation of shareholder directors in the selection committee for selection of Managing director

Governing Boards and Directors



Gap

- ◉ FMC norms require governing board to include Independent Director, Shareholder Director and MD
- ◉ FMC has not defined these set of entities
- ◉ Unlike Stock Exchange, there is no restriction for trading members or their associates and agents to nominate shareholder director (NCDEs). As RCDEs are not demutualised, their governing boards include directors who are brokers.
- ◉ FMC prescribes that the Chairperson of the Board of Directors of the Exchange shall be an Independent Director and shall be appointed with the prior approval of the Commission. There is no reference to election of chairperson by the Governing Board.

Governing Boards and Directors



Gap

- For quorum, the presence of public interest director is not required in FMC
- As per FMC, Independent Directors can be appointed for a maximum of 2 terms of 3 years each.
- As per FMC norms, the committee for selection of Managing director should have representation of two Shareholder Directors.

Proposals (Issuance of Circular)

- Existing Independent directors on the board may be deemed to be PIDs under SECC.
- Any new appointments on governing boards of NCDEs may be subject to compliance with SECC and SEBI circular dated December 13 2012. Existing directors of NCDEs who are not in compliance with SECC may be allowed to continue for 1 year from merger or till completion of the term, whichever is earlier.
- RDCEs may comply with the requirements of Regulation 23 to 26 within 3 years from the date of merger

Compensation Policy



Gap

- As per SECC, Regulation 27 prescribes norms of compensation policy for KMP
- As per FMC, No such norms on compensation policy given

Proposal (Issuance of Circular)

- It is proposed to allow NCDEs one year time and RCDEs time line co-terminus with that provided for corporatization and demutualization, to comply with this requirement.

Segregation of Regulatory Department



Gap

- As per SECC, Regulation 28 stated stock exchange shall adopt a 'Chinese wall' policy which separates the regulatory departments of the recognised stock exchange from other departments
- As per FMC, No such requirements for segregating the regulatory department from other departments

Proposal (Issuance of Circular)

- It is proposed to allow CDEs 6 months to comply with this requirement

Oversight Committees

Gap

- As per SECC, Regulation 29 mandate stock exchange to constitute following oversight committees of the governing board, each chaired by a public interest director, in address the conflict of interest: Member regulation, Trading & surveillance function
- FMC has no requirements of oversight committees

Proposal

- it is proposed that CDEs may not be required to constitute oversight committee for listing functions.
- Issuance of circular, All CDEs may be required to constitute oversight committee within 3 months from the date of merger

Advisory Committee



Gap

- As per SECC, Regulation 30 mandate stock exchange to constitute Advisory committees of the governing board to advise the governing board on non regulatory and operational matters including product design, technology, charges & levies.
- Comprises of its trading members and the chairperson of the governing board shall be the head of Advisory committee and the MD shall be a permanent invitee to every meeting.
- FMC has no requirements of Advisory committee

Proposal (Issuance of Circular)

- it is proposed that NCDEs may be given 1 year from the date of merger and RCDEs time line co-terminus with that provided for corporatization and demutualization

Risk Management committee



Gap

- As per SECC, Regulation 31 requires recognized clearing corporations to constitute risk management committee
- FMC has directed NCDEs to constitute risk management committee.

Proposal (Amendment to SECC)

- As the functions of clearing and settlement are being carried out by the exchanges themselves, it is proposed to mandate CDEs to constitute risk management committee in terms of Regulation 31 immediately.

Appointment of Compliance Officer



Gap

- As per SECC, Regulation 32 requires appointment of compliance officer who shall be responsible for monitoring the compliance of the SCRA, Companies Act 1956, SEBI 1992, rules, regulations or directions issued there under and for redressal of investor grievances
- As per FMC, There is no stipulation of appointment of compliance officer

Proposal (Issuance of Circular)

- CDEs may be required to appoint compliance officer in terms of Regulation 32.

Transfer of Penalties

Gap

- As per SECC, Regulation 34 requires to credit the penalties levied by it to Investor Protection Fund (IPF) and clearing corporations to credit the penalties levied by it to the fund to guarantee settlement of trades(SGF)
- As per FMC, NCDEs have both IPF & SGF, but RCDEs have SGF only. FMC has mandated NCDEs to credit settlement trade penalties to their SGF and all other penalties to IPF

Proposal (Amendment to SECC)

- It is proposed to mandate NCDEs to comply with the requirement of FMC and advise RCDEs to credit all the penalties to SGF till the creation of IPF

Disclosure and Corporate Governance Norms



Gap

- For stock exchanges, SEBI has mentioned that disclosure requirements and corporate governance norms would be in line with the requirements for listed companies (Regulation 35)
- FMC has mandated exchanges to comply with the norms of Companies Act, 2013.

Proposal (Issuance of Circular)

- After the merger of FMC with SEBI, the NCDEs may be required to comply with the corporate governance norms. RCDEs may be required to comply with this requirement within three years from the date of merger.

General Obligations

Gap

- As per SECC, Regulation 36 requires stock exchange to use services of clearing corporation for clearing and settlement of trades
- Regulations 37 to 44 are general obligations for stock exchanges and clearing corporations (agreement between stock exchange and clearing corporation, SEBI approval for admission of securities for clearing, fund to guarantee settlement of trades, utilization of profits and investments by clearing corporation, provide fair and transparent access, not to engage in unrelated activity except through separate legal entity, maintenance of books of accounts and records, submission of annual financial statements and returns, bye-laws and rules)
- Regulations 44A and 44B pertain to settlement and netting and rights of clearing corporation to recover dues.

General Obligations

Gap

- As per FMC, CDEs clear and settle their clearing house. As it is proposed to permit CDEs to continue their present arrangement of clearing & settlement.
- Regulations 36 to 40, 41(1) & 44 AB would not be applicable to CDEs

Proposals (Amendment to SECC)

- CDEs may be allowed to continue their present arrangement of clearing & settlement of trades for a period not exceeding 3 years from merger date
- Regulation 39 (fund to guarantee settlement of trades) may be made applicable to NCDEs & CDEs.
- Regulation 44B, right of clearing corp to recover their dues against the members be made applicable to CDE
- CDEs may not be permitted to engage in any other activity of assisting, regulating or controlling the business of buying, selling or dealing in CDEs except with prior permission of SEBI

General Obligations

Proposals (Issuance of Circular)

- Regulations 41(2) (providing fair access), 41(3) (not to engage in unrelated activity except through separate legal entity), 42 (maintenance of books of accounts and records), 43 (Submission of annual financial statements and returns), 44 (bye-laws, rules) and 44A (settlement and netting) may be made applicable to CDEs.

Listing of Securities



Gap

- As per SECC, Regulation 45 pertains to listing of securities of recognized stock exchange
- Regulation 46 requires that securities of a recognised stock exchange shall be in dematerialised form
- FMC has permitted listing of securities of NCDEs on stock exchanges.
- There is no requirement as far as FMC is concerned (Regulation 46)

Proposals(Issuance of Circulars)

- Application of Regulation 45 from the date of merger
- NCDEs may be given 6 months and RCDEs may be given 3 years from the merger date to comply with regulation 46- dematerialization of securities

Arbitration mechanism and Investor Redressal Mechanism



Gap

As compared to securities market, there are gaps of:

- Non availability of a web based centralized system for registering investor complaints against brokers and monitoring of the same.
- Absence of Investor Grievance Redressal Committee (IGRC) to decide the admissible claim value and guidelines for broking/ releasing such admissible amount from the deposit of the trading member
- Absence of detailed/comprehensive guidelines on maintaining panel of arbitrators, appointment of arbitrators, jurisdiction of arbitration, timelines for disposal of arbitration references, timelines prescribed for appointment of arbitrator(s), common pool of arbitrators, automatic process of selection of arbitrators in case neither of the parties agree on names of arbitrators.
- Absence of detailed / comprehensive guidelines regarding the manner, fees and timelines for implementation of arbitration award.

Arbitration mechanism and Investor Redressal Mechanism



Proposals (Issuance of Circular)

- For Web Based centralized online platform- Introduction of SCORES(SEBI Complaint Redressal System)
- To constitute IGRC at NCDEs and empower the committee to decide the admissibility of investors claims and also give monetary relief to the investors
- To prescribe detailed/comprehensive guidelines on maintenance of panel, appointment etc of arbitrator
- To expand the number of Investor Services Centres'(ISCs) of the CDEs in order to facilitate the investors to take up their grievance. NCDEs may comply with the same within timelines prescribed by SEBI
- To prescribe detailed / comprehensive guidelines regarding the manner, fees and timelines for implementation of arbitration award.
- To introduce appellate arbitration mechanism at NCDEs.

Allotment of Codes

Gap

- SEBI assigned codes to stock exchanges in the country. It is a two digit code which is incorporated in the twelve digit registration number given to the trading members.
- For CDEs, SEBI needs to issue code which become deemed recognized stock exchanges.

Proposal

- It is proposed that SEBI may assign code to all CDEs which become deemed stock exchanges consequent to merger, on the date of merger.

Thank You