BEFORE THE ADJUDICATING OFFICER

SECURITIES AND EXCHANGE BOARD OF INDIA

[ADJUDICATION ORDER NO.: - SD/AO/03/2012]

UNDER SECTION 15-I OF SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 READ WITH RULE 5 OF SEBI (PROCEDURE FOR HOLDING INQUIRY AND IMPOSING PENALTIES BY ADJUDICATING OFFICER) RULES, 1995

Against

M/s. Ess Ess Intermediaries Pvt. Limited
PAN: AAACE7722Q

BRIEF FACTS OF THE CASE:

1. Securities and Exchange Board of India (hereinafter referred to as 'SEBI') had initiated investigation in the scrip of M/s. Adani Exports Limited (hereinafter referred to as 'AEL'), a public company mainly traded on the Bombay Stock Exchange (hereinafter referred to as the 'BSE') and the National Stock Exchange (hereinafter referred to as 'NSE'), to examine the possibility of violation of provisions of various SEBI Regulations in respect of trading in the scrip for the period from between July 09, 2004 and January 14, 2005 (hereinafter referred to as the first period) and August 08, 2005 to September 09, 2005 (hereinafter referred to as the Second Period). The price of the scrip witnessed huge spurt in volumes and wide fluctuations in the price ranging from 481 to 756 (during pre split in first period) and from Rs. 64.35 to Rs. 74.20 (during the second period).

2. The role of the brokers and their clients who had traded in the scrip of AEL were scrutinized. It was alleged that through collusion with the brokers and other clients, certain entities transacted in the shares of AEL in such a

manner that led to creation of artificial volumes in the scrip and was designed to create a false market and distorted market equilibrium leading to spurt in the price of the scrip which did not have any correlation with the performance of the company.

3. It was alleged that one of the sub-brokers, viz., M/s Ess Ess Intermediaries Pvt. Ltd. (hereinafter referred to as **"the Noticee"**), trading for its client Shri Nitin Patel (hereinafter referred to as **"said client"**) violated the provisions of Regulations 4(1), 4(2)(a), (b), (e), (g) and (n) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Markets) Regulations, 2003 (hereinafter referred to as **"PFUTP Regulations"**) and clauses A(1), A(2), D(1), D(4) and D(5) of the Code of conduct as specified in the schedule II under Regulation 15 of the SEBI(Stock Brokers and Sub–Brokers) Regulations,1992 (hereinafter referred to as the **"Broker Regulations"**) and was therefore, liable for monetary penalty under section 15HA and 15HB of Securities and Exchange Board of India Act, 1992 (hereinafter referred to as "**SEBI Act**").

APPOINTMENT OF ADJUDICATING OFFICER:

4. Ms. Babita Rayudu was appointed as Adjudicating Officer vide order dated July 24, 2007 under section 15 I of SEBI Act read with rule 3 of SEBI (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules, 1995 (hereinafter referred to as **'Rules'**) to inquire into and adjudge the aforesaid alleged violations committed by the Noticee.

5. Subsequent to the transfer of Ms. Babita Rayudu, the undersigned was appointed as the Adjudicating Officer vide order dated November 23, 2007.

SHOW CAUSE NOTICE/REPLY/PERSONAL HEARING:

6. Accordingly, a notice to show cause dated June 20, 2008 under Rule 4 (1) of the Rules was issued to the Noticee asking it to show cause as to why an enquiry should not be held against it in terms of Section 15I of the SEBI Act and penalty be not imposed under Section 15HA and 15HB of the SEBI Act for the alleged violation by it of the abovementioned provisions of the PFUTP Regulations and the Broker Regulations.

7. In response to the said notice to show cause (hereinafter referred to as the 'SCN'), the Noticee vide letter dated July 5, 2008 sought an extension of 30 days to file the reply.

8. In the interest of natural justice and in order to conduct an inquiry as per rule 4 (3) of the Rules, the Noticee was granted as opportunity of personal hearing before me on August 3, 2009. The Noticee vide letter dated July 25, 2009 informed that it had filed for consent and to keep the proceedings in abeyance. The Noticee vide letter dated August 1, 2009 submitted its reply to the SCN. In the course of hearing the Noticee sought time till August 31 to file a detailed reply. The Noticee vide letter dated August 31, 2009 submitted that it needed certain documents to file a detailed reply. The Noticee was provided all the relevant documents vide Notice dated February 10, 2009 and granting another hearing to the Noticee on February 24, 2010. The Noticee attended the said hearing through its authorized representatives (hereinafter referred to as the 'AR') and submitted that it would file a detailed reply by March 26, 2010. However, the Noticee failed to make any submissions till date.

CONSIDERATION OF ISSUES AND FINDINGS:

9. I have carefully perused the charges against the Noticee mentioned in the SCN, the submissions of the Noticee and the documents available on record. The issues that arise for consideration in the present case are stated and determined, one by one, as follows:

- **Whether the Noticee has violated Regulation 4 (1) and 4 (2) (a), (b), (e),(g) and (n) of the PFUTP Regulations, 2003?**

10. Before proceeding to decide the above issue, it is important to have a look at the abovementioned provisions as they existed at the relevant time, which interalia are reproduced below.

"4. Prohibition of manipulative, fraudulent and unfair trade practices

(1) Without prejudice to the provisions of regulation 3, no person shall indulge in a fraudulent or an unfair trade practice in securities.

(2) Dealing in securities shall be deemed to be a fraudulent or an unfair trade practice if it involves fraud and may include all or any of the following, namely :—

(a) indulging in an act which creates false or misleading appearance of trading in the securities market;

(b) dealing in a security not intended to effect transfer of beneficial ownership but intended to operate only as a device to inflate, depress or cause fluctuations in the price of such security for wrongful gain or avoidance of loss;

…

(e) any act or omission amounting to manipulation of the price of a security;

…

(g) entering into a transaction in securities without intention of performing it or without intention of change of ownership of such security;"

…

(n) circular transactions in respect of a security entered into between intermediaries in order to increase commission to provide a false appearance of trading in such security or to inflate, depress or cause fluctuations in the price of such security;

11. As per the findings of the Investigation Report (hereinafter referred to as the 'Report') pertaining to the said investigation, the analysis of the price-volume data of the scrip of AEL for the period under investigation revealed that the price of the scrip had witnessed wide fluctuations in the price ranging from 481 to 756 (during pre split in first period) and from Rs. 64.35 to Rs. 74.20 (during the second period). It was observed that average volumes in the scrip witnessed significant rise during the investigation period.

12. During the course of the said investigation, it was observed that the Noticee was one of the sub-brokers who had traded substantially in the scrip of AEL during the first and the second period for the said client. The Noticee, for the said client, has allegedly executed synchronized trades for 1,15,870 shares of AEL during the period from July 9, 2004 to July 27, 2004. Further, the said client also entered into self trades for 52,910 shares. The said client also entered into structured trades wherein he reversed the trades with particular clients of other brokers. A total trading of 1,29,422 shares was executed by the said client in such manner between July 16, 2004 and July 27, 2004. This quantity accounted for 12.5% of the total traded quantity during this period. It is further observed that during the period between July 28, 2004 to January 14, 2005 the said client is alleged to have entered synchronized trading for buying 83,45,924 shares and selling 87,60,410 shares. The said client was part of the group which executed trades of 3,48,53,139 shares during the above period which is around 51% of total traded volumes. Of these trades 3,04,68,762 shares (87.39 % of their trades) appear to be synchronized.

13. It is further alleged that the said client along with few other entities executed reverse trades to the extent of 38,21,269 shares during the second period. It is alleged that the said client along with few other entities traded in a manner such that orders for 28,22,240 shares appear to be synchronized as the buy and sell orders were placed within time gap of 1

minute. Moreover, for 18,38,077 shares buy and sell order quantity and rate identical and placed within a time gap of 1 minute from each other. In case of 116 trades for 2183102 shares the time gap between the buy and sell orders was between 0-10 seconds. The said client's contribution to the alleged manipulation is to the extent of 13,21,582 shares on buy side and 15,04,408 on the sell side. Similarly on NSE, for the same period the said client has allegedly entered into synchronized trades to the extent of 12,25,260 shares.

14. It is alleged that the said trades were synchronized as the buy and sell orders were placed within time gap of 1 minute with negligible or no price difference. Further, these trades have been reversed on the same day. These trades were allegedly done with a view to increase the price of the scrip and create artificial volumes and consequently create artificial demand in the scrip. It is further alleged that the Noticee, by executing the said trades on behalf of the said client, had aided and facilitated manipulation in the scrip. This allegation is substantiated by the fact that the said client was doing trading in huge volume and was reversing it on the same day. There has been negligible change in the beneficial ownership because of the trading done by the said client and the trading done by said client has only contributed to the increase in the price and volume of the scrip of AEL. The orders placed by the said client used to be identical in terms of price and quantity and used to be placed with negligible price difference.

15. In response of the said allegation of structured trades, the Noticee submitted that the said transactions were carried out by the client in normal course of business and there is nothing on record to show that the Noticee had knowledge of manipulative intention of the said client. Further, synchronized trading and reversal trading are not illegal per se.

16. In order to determine whether the Noticee has executed these transactions with a fraudulent purpose, there are various factors which have to be considered. The Hon'ble SAT in the matter of *Ketan Parekh v. Securities and Exchange Board of India*, *Appeal no. 2 of 2004,* has held that

"…*Any transaction executed with the intention to defeat the market mechanism whether negotiated or not would be illegal. Whether a transaction has been executed with the intention to manipulate the market or defeat its mechanism will depend upon the intention of the parties which could be inferred from the attending circumstances because direct evidence in such cases may not be available.* ***The nature of the transaction executed, the frequency with which such transactions are undertaken, the value of the transactions, whether they involve circular trading and whether there is real change of beneficial ownership, the conditions then prevailing in the market are some of the factors which go to show the intention of the parties****. This list of factors, in the very nature of things, cannot be exhaustive. Any one factor may or may not be decisive and it is from the cumulative effect of these that an inference will have to be drawn."*

It is observed that the trading done by the said client was huge and the Noticee should have been alarmed by the trading being executed by the client. Even if the client was doing day trading, such pattern of trading still remains unexplained. The said client had entered the orders with precise timing, quantity and price. Such preciseness could not be achieved unless there is an understanding between the Noticee and the said client. The fact that the said client has reversed his trading and has entered into self trades shows that the clients activities could not be considered to be normal by any prudent standard. Further, the Noticee has failed to submit

any detailed submissions in response to SCN even after providing it with all the necessary materials and providing it adequate opportunities.

17. In view of the above observations, findings and material on record I conclude that the allegation of violation of Regulation 4 (1) and 4 (2) (a), (b),(e),(g) and (n) of the PFUTP Regulations, 2003 by the Noticee is proved.

- **Whether the Noticee has violated Regulation A(1), A(2), D(1), D(4) and D(5) of the Code of conduct as specified in the schedule II under Regulation 15 of the Broker Regulations ?**

18. Before proceeding to decide this issue, it is necessary to have a look at the abovementioned provisions, as they existed at the relevant time. The same are reproduced below:

SCHEDULE II

CODE OF CONDUCT FOR SUB-BROKERS

A. General.

(1) Integrity: A sub-broker, shall maintain high standards of integrity, promptitude and fairness in the conduct of all investment business.

(2) Exercise of due Skill and Care : A sub-broker, shall act with due skill, care and diligence in the conduct of all investment business.

D. Sub-Brokers vis-à-vis Regulatory Authorities

(1) General Conduct: A sub-broker shall not indulge in dishonourable, disgraceful or disorderly or improper conduct on the stock exchange nor shall he wilfully obstruct the business of the stock exchange. He shall comply with the rules, bye-laws and regulations of the stock exchange.

(4) Manipulation: A sub-broker shall not indulge in manipulative, fraudulent or deceptive transactions or schemes or spread rumours with a view to distorting market equilibrium or making personal gains.

(5) Malpractices: A sub-broker shall not create a false market either singly or in concert with others or indulge in any act detrimental to the public interest or which leads to interference with the fair and smooth functions of the market mechanism of the stock exchanges. A sub-broker shall not involve himself in excessive speculative business in the market beyond reasonable levels not commensurate with his financial soundness.

19. It is alleged that the Noticee had executed the said transactions on behalf of the said client. The trading of the said client, in the scrip of AEL, with the Noticee seems to be rather unusual as he has mostly squared up his position mostly on intra day basis without much profit/loss. The trading of client for such huge volume that too on an intraday basis without gaining much is rather unusual. Further, the orders placed by Noticee got executed almost instantaneously. The Noticee as a broker of the said client should have got suspicious and raise concerns over such pattern of trading. However, the Noticee failed to raise any concern over the suspicious trading pattern of the said client. The Noticee is a registered sub-broker and as a specialized intermediary a higher standard of care and diligence is expected from the Noticee. The Noticee has miserably failed in executing its duties and was unable to keep a check on its client.

20. In view of the abovementioned observations and findings and all the material on record, I am of the opinion that the allegation of violation of Clauses A(1), A(2), D(1), D(4) and D(5) of the Code of conduct as specified in the schedule II under Regulation 15 of the Broker Regulations is proved.

LEVY OF PENALTY

21. The Hon'ble Supreme Court of India in the matter of *SEBI Vs. Shri Ram Mutual Fund* [2006] 68 SCL 216(SC) held that *"In our considered opinion, penalty is attracted as soon as the contravention of the statutory obligation as*

contemplated by the Act and the Regulations is established and hence the intention of the parties committing such violation becomes wholly irrelevant…".

22. Thus, the violation of Regulations 4(1), 4(2)(a), (b), (e), (g) and (n) of PFUTP Regulations and clauses A(1), A(2), D(1), D(4) and D(5) of the Code of conduct as specified in the schedule II under Regulation 15 of the Broker Regulations by the Noticee, make it liable for penalty under section 15HA and 15 HB of SEBI Act, 1992 respectively which reads as follows:

"15HA. Penalty for fraudulent and unfair trade practices.

If any person indulges in fraudulent and unfair trade practices relating to securities, he shall be liable to a penalty of twenty-five crore rupees or three times the amount of profits made out of such practices, whichever is higher."

15HB.Penalty for contravention where no separate penalty has been provided.-

Whoever fails to comply with any provision of this Act, the rules or the regulations made or directions issued by the Board thereunder for which no separate penalty has been provided, shall be liable to a penalty which may extend to one crore rupees.

23. In view of the foregoing, I am convinced that it is a fit case to impose monetary penalty under section 15 HA and 15 HB of the SEBI Act.

24. While determining the quantum of penalty under section 15HA, it is important to consider the factors stipulated in section 15J of SEBI Act, which reads as under:-

*"**15J - Factors to be taken into account by the adjudicating officer***

While adjudging quantum of penalty under section 15-I, the adjudicating officer shall have due regard to the following factors, namely:-

(a) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default;

(b) the amount of loss caused to an investor or group of investors as a result of the default;

(c) the repetitive nature of the default."

25. In the present matter it is difficult to quantify the gain made by the Noticee or the loss caused to the investors. However, It is observed that the Noticee failed to exercise due diligence and has aided and abetted the said client because of which the said client was able to indulge in the abovementioned manipulation for his personal gains in the scrip of AEL. Even if the Noticee had not received any disproportionate gain or unfair advantage due to the said manipulation, the same has surely harmed the integrity of a fair and open market and has caused loss to the innocent investors.

ORDER

26. After taking into consideration all the facts and circumstances of the case, I hereby impose a penalty of ₹ 9,00,000/- (Rupees Nine Lakhs only) under section 15HA of SEBI Act on the Noticee, M/s Ess Ess Intermediaries Pvt. Ltd. for the violation of Regulations 4(1), 4(2)(a), (b), (e), (g) and (n) of PFUTP Regulations and ₹ 1,00,000/- (Rupees One Lakh only) under section 15HB of SEBI Act on the Noticee for the violation of clauses A(1), A(2), D(1), D(4) and D(5) of the Code of conduct as specified in the schedule II under Regulation 15 of the Broker Regulations. The total penalty thus levied on the Noticee is ₹ 10,00,000/- (Rupees Ten lakhs

only). In my view, this penalty is commensurate with the violations committed by it.

27. The Noticee shall pay the said amount of penalty by way of demand draft in favour of "SEBI - Penalties Remittable to Government of India", payable at Mumbai, within 45 days of receipt of this order. The said demand draft should be forwarded to Division Chief, Investigation Department, ID-1, Securities and Exchange Board of India, SEBI Bhavan, Plot No. C – 4 A, "G" Block, Bandra Kurla Complex, Bandra (E), Mumbai – 400 051.

28. In terms of rule 6 of the Rules, copies of this order are sent to the Noticee and also to SEBI.

Date: **December 14, 2012**
Place: **Mumbai**

Sandeep Deore
Adjudicating Officer