BEFORE THE ADJUDICATING OFFICER

SECURITIES AND EXCHANGE BOARD OF INDIA

(ADJUDICATION ORDER NO: AO/SBM/EAD-1/05/2019)

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

In respect of:

M/s Shilpa Stock Brokers Pvt Ltd
PAN: AAECS9799R
No 5, Natwar Chamber, No. 94
Nagindas Master Road
Fort, Mumbai 400 001
In the matter of

Trading in the F & O segment at NSE

FACTS OF THE CASE

1. During the period from 1st February 2005 to 31st March, 2005, alerts were generated at the National Stock Exchange ('**NSE'**) identifying trading pattern in the options contracts having price variation, low volumes and / or no major change in the open interest position. On the basis of these alerts, it was observed by NSE that the trading members were buying and selling almost equal quantities during the day. NSE had observed that the trades of the trading members in the option contracts appeared to be synchronized and one of the parties to the transaction apparently had a positive close out difference, whereas the other party to the transaction had a negative close out difference. The report submitted by NSE had also observed that the matched transactions and their close-out transactions were executed in various options contracts on different underlying with no or small outstanding open interest position. It was further observed by NSE that the

reversal/close out transactions were executed at significantly varying prices within a short period of time.

2. Based on the above observations brought out by NSE, Securities and Exchange Board of India (**'SEBI'**) conducted an investigation into the dealings in the futures and options segment of NSE, during the period February 1, 2005 to March 31, 2005 (hereinafter referred to as '**investigation period'**). Upon analysis of the trade and order log w.r.t the options contracts executed during the investigation period, it was observed by SEBI that various combinations of trading members were executing the transactions amongst themselves, either in their own account and/ or on behalf of their clients or both. It was also observed during the course of investigation that the same quantity and in few cases, substantially the same quantity of the original trade was closed out during the day at a price (premium for option contracts), which was significantly above or below the price at which the first/original transaction in the option contract was executed, the strike price being the same. It was observed that most of these trades had a time difference of less than 1 second between the buy and sell orders, remaining trades were invariably executed within few seconds i.e were executed at less than 60 seconds. It was also observed by SEBI that these trades were synchronized in nature and one of the parties to the transaction had a positive close-out difference whereas, the other party had a negative close-out difference. Therefore, it was concluded by SEBI that these transactions were reversal trades and were non-genuine transactions that were executed by the Trading Members in collusion with certain clients/entities and other stock brokers.

3. During the course of investigations, it was observed by SEBI that M/s Shilpa Stock Brokers Pvt Ltd (hereinafter referred to as '**Noticee' / 'SSPL'**) had executed trades in the options segment during the aforementioned investigation period and had allegedly colluded with its clients and other stock brokers to execute reversal/ non-genuine transactions in the futures and options segment of NSE. Based on the findings of the investigations, it was alleged that certain irregularities / fraudulent dealings were committed by the Noticee in connivance with its clients,

resulting into the misuse of the options segment at NSE during the above referred investigation period. It was further observed that the Noticee who had traded in its proprietary account was a counter-party to all these transactions that were executed during the investigation period. Therefore, it is alleged that Noticee has failed to exercise skill, care, and diligence in the conduct of its business as a stock broker while executing these transactions in the options segment in its proprietary account and also on behalf of its clients during the investigation period. It is alleged that the transactions executed by the Noticee in its proprietary account and also on behalf of its clients in the options segment were reversed more or less immediately after the original transaction at a significantly high close out difference. Thus, it is alleged that the transactions undertaken by the Noticee in the options contracts were non-genuine and the market mechanism was ostensibly misused for such fraudulent purposes.

4. In view of the above observations, it is alleged that Noticee has violated the provisions of Regulations 4(1), 4(2)(a), 4(2)(b), 4(2)(e), 4(2)(g) and 4(2)(n) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (hereinafter referred to as '**PFUTP Regulations'**) and also the provisions of Clauses A(1), A(2), A(3), A(4) and A(5) of the Code of Conduct prescribed for Stock Brokers contained in Schedule II under Regulation 7 of the SEBI (Stock Brokers and Sub- Brokers) Regulations, 1992 (hereinafter referred to as **'Stock Broker Regulations'**). SEBI has, therefore, initiated adjudication proceedings against the Noticee under the provisions of sections 15HA and 15HB of the SEBI Act, 1992 (hereinafter referred to as '**SEBI Act'**) for the aforementioned alleged violation of the provisions of law by the Noticee.

APPOINTMENT OF ADJUDICATING OFFICER

5. Shri D Ravikumar was appointed as Adjudicating Officer, vide Order dated July 29, 2009 under Section 15-I of the SEBI Act read with Rule 3 of SEBI (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules, 1995 (hereinafter referred to as '**Adjudication Rules'**) to inquire into and adjudge under the provisions of sections 15HA and 15HB of the SEBI Act for the aforementioned

alleged violation of the provisions of law by the Noticee. Subsequently, the undersigned has been appointed as the Adjudicating Officer ('AO') in the matter vide Order dated June 22, 2015.

SHOW CAUSE NOTICE, REPLY AND PERSONAL HEARING

6. Show Cause Notice (hereinafter referred to as '**SCN**') dated September 16, 2009 was issued to the Noticee. The SCN was issued to the Noticee under the provisions of Rule 4 (1) of the Adjudication Rules, to show cause as to why an inquiry should not be held against it and why penalty should not be imposed on the Noticee for the aforementioned alleged violation of the provisions of law by the Noticee. The SCN issued to the Noticee, *inter-alia*, mentioned the following:-

   a) *SEBI conducted an investigation into the dealings in the futures and options segment of NSE, during the period from 1st February 2005 to 31st March 2005. It is alleged on the basis of the findings of the investigation report that, during the said period, Noticee had executed non-genuine transactions in collusion with certain clients and brokers in the futures and options segment of NSE.*

   b) *It is alleged that during this period, Noticee bought and sold almost equal quantity of contracts within the day and such buy / sale transactions were synchronized in nature. By executing the said trades, the original trades were closed out during the day at a price which was significantly above or below the price at which the first / original transaction was executed, without any significant variations in the traded price of the underlying security.*

   c) *It was alleged that one of the parties to each of the transactions had a positive close out difference whereas the other entity had a negative close out difference, effectively resulting in reversal of trades. Most of these trades had a time difference of 0-60 seconds between the buy and sell orders.*

d) The summary of the alleged fraudulent trades done by the Noticee is given below:

Members Name	***Gross Traded Value (in Rs. lakh)***	***Close out difference amount (in Rs. lakh)***	***Whether for Clients/ Own Account***	***Cross/ structured deals***
Shilpa Stock brokers Pvt Ltd	*132.94*	*40.23*	*Own account /Clients*	*Cross*

e) The above stated actions amount to non-genuine trades and misuse of the options segment of the market for ulterior motives and are in violation of Regulations 4(1), 4(2)(a), 4(2)(b), 4(2)(e), 4(2)(g) and 4(2)(n), of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003.

f) It is further noted that that on March 10, 2005, NSE had issued a circular NSE/INVG/2005/04 to brokers, inter-alia, specifically advising them to desist from entering such transactions, as detailed above, as well as orders which, prima facie, appear to be non-genuine on their own account and / or on behalf of their clients. Further, it is also alleged that Noticee has violated the Clauses A(1), A(2), A(3) A(4) and A(5) of the code of conduct prescribed for Stock brokers in Schedule II under Regulation 7 of SEBI(Stock Brokers and Sub- Brokers) Regulations, 1992.

7. In its initial response to the SCN, Noticee vide its letter dated May 29, 2009 informed that it had filed for the settlement of the adjudication proceedings through consent mechanism with SEBI. Thereafter, vide an internal communication dated April 13, 2010, the concerned department of SEBI (i.e DRA II) informed that the settlement application filed by the Noticee has been rejected by the High Powered Advisory Committee ('HPAC'). Subsequently, during the course of the present proceedings, another communication dated April 26, 2018 was received from EFD

II wherein it was mentioned that Noticee has once again filed a settlement application in the said matter. Thereafter, vide communication dated October 04, 2018 received from EFD II, it was informed that the said settlement application filed by the Noticee has been rejected as the Noticee failed to submit the revised settlement terms, as instructed by the internal committee (IC).

8. The Noticee's reply to the SCN, vide its letter dated August 17, 2010, *inter alia*, mentioned the following: -

   a) *The said notice alleges in the para under reply that during the said period various combinations of trading members, including us, were executing transactions among themselves, on own account or on behalf of their clients or both. In this regard, while denying the allegations we state and submit that said allegations of executing the trades in combinations are vague and ambiguous. We further deny that any non-genuine trades were executed during the said period. The show cause notice fails to establish the nature of combinations in a clear manner.*
   b) *Further, we submit that no evidence has been provided to us to indicate that the trades executed during the said period were synchronized in nature except for the reasons that almost equal quantities of contract were bought and sold within the day.*
   c) *It is alleged that by executing the said trades, the original trades were closed out during the day at a price which is significantly above or below the price at which the first/original transaction was executed without significant variations in the underlying securities. Most of this trades had a time difference of 0 to 60 seconds between the buy and sell order. We submit that as far as we are concerned we deny that the above stated action amounts to non-genuine case and mis-use of market for ulterior motives. We state and submit that we have executed the trades on behalf of our clients under their instructions for the sole purpose of earning brokerage. As far as we are concerned, the alleged trades were genuine so far as they*

were permissible by exchange, within the price brand of the day and the differences were paid for.

d) *It is also alleged that one of the party to the transaction had positive close out difference whereas other had the negative close out difference which is quite normal in F & O trades. The trades were executed during the usual course of business and we deny that there were any reversal of trades.*

e) *It is earnestly submitted that a genuine transaction by itself cannot attract the provisions of the PFUTP Regulations even if such a transaction had resulted in volume and price variation. We state that the PFUTP Regulations may be attracted only if the transaction is made with an intention to artificially raise or depress the prices of securities so as to induce any other person to sell or purchase the securities. The investigating officer has failed to produce any instance of the same.*

f) *With respect to observance of due diligence we submit that we have maintained high standards of integrity, promptitude and fairness in the conduct of all our business. We had obtained proper "know my client form/ agreement" as prescribed, duly filled in the required details, inter alia, containing specific details such as Client Code, address etc. It is submitted that we had taken all care, which is required to be taken about the creditability of the client for payment and his capacity to trade in the market. As a stock-broker, we believe that we have exercised proper due diligence at the time of the registration of the client by knowing the client and subsequently ensuring that the client is not fictitious, by way of assuring that payments are received and made by account payee cheques, shares received and delivered into proper demat accounts and that our client deal in fundamentally sound companies, etc. .*

g) *We state and submit that a Broker is bound by the Code of Conduct as prescribed in SEBI (Stock Brokers and Sub brokers) Regulations, 1992. When a client instructs a broker, the Broker has no other option but to buy/ sell, in the absence of any knowledge about the wrong doing by the client, pre or post trading. If the broker fails to carry out the instructions of the*

client, then the same results in breach of the provisions of the Code of Conduct by the Broker and entails penal consequences.

h) *We submit that simply because our gross traded value during the period of investigation in the matter of dealings in futures and options segment of National Stock Exchange in our own account and on behalf of some clients was Rs. 132.94 lacs with close out amount difference of 40.23 lacs (as per annexure "A" of the show cause notice) does not and cannot by any stretch of imagination make the trades manipulative. Further, in absence of any specific details we are not in position to verify the said fact. Our above contention is on assumption, without admission of having executed the alleged trades.*

i) *Further, we have entered orders on the online system of the Exchange which ensures transparency. When an order is entered in the automated trading mechanism of the Stock Exchange, the order can be picked up by anyone. The trading mechanism is so fast that the orders get converted into trades in a fraction of second. In the automated price and order matching mechanism of the trading system, it is impossible for a stock-broker to know the counter party of his trade.*

j) *At the outset, we state that an order dated 18.06.2007 (hereinafter referred as earlier SCN) of Ld. WTM Shri Anantharaman was served on us which was followed by Notice dated 05th October 2007 (hereinafter referred to as the said earlier notice) under Rule 4 by the Ld. AO Shri Biju S. We state that the said earlier notice had detailed out the purported violations which were for the period January 2007 to March 2007. We had opted for consent proceedings against the same and therefore the enquiry proceedings against us may be deemed as concluded ad disposed of. Subsequently, we had never indulged into any further violations and therefore the present SCN which is for an earlier period i.e. from 1st February 2005 to 31st March 2005 appears to be an act subsequent to our already having suffered the alleged violations. It is pertinent to note that the present SCN under reply seems to be for a period which is later than the period of the earlier notice wherein the*

allegations appear to be of similar nature. We respectfully submit that since the earlier notice had been concluded on the basis of our consent proposal, we had subsequently been extra diligent and had never indulged in any further purported irregularities or violations. Therefore, a favorable view of the matter be taken.

9. In the interest of natural justice and in order to conduct an inquiry in terms of Rule 4(3) of the Adjudication Rules, Noticee was provided with an opportunity of personal hearing on February 08, 2011. On the stipulated date of hearing, Mr. Somasekhar Sunderashan, Mr Paras K. Parekh, Advocate, Mr. Gopal Lal Maliwal and Mr. Rakesh Nahar, Directors of the Noticee (hereinafter referred to as **'ARs'**) appeared on behalf of the Noticee and reiterated the submissions made by the Noticee vide its letter dated August 17, 2010. The ARs further stated that the Hon'ble Securities Appellate Tribunal (hereinafter referred to as ' **SAT** ') in the matter of Rakhi Trading Pvt Ltd vs SEBI has observed that only such synchronised trades that violate the relevant regulations and manipulate the market are violative of the PFUTP Regulations and in present case, the ARs stated that the impugned trades have not resulted in price manipulation. The ARs also referred to the Order of Hon'ble SAT in the matter of Indiabulls Securities Ltd vs SEBI and a judgment of the Hon'ble Supreme Court in the matter of Union of India vs Kamalakshi Finance Corporation Ltd. Subsequent to the aforementioned hearing, the Noticee also submitted a letter dated March 14, 2011, primarily reiterating its earlier submissions made vide its letter dated August 17, 2010.

10. Pursuant to my appointment as AO in the matter, the Noticee was provided with opportunities of hearing on September 28, 2016 and on January 18, 2019. Shri Prakash Shah, Shri Anil Maliwal and Shri Robin Mahesh Shah had appeared as the Authorised Representatives on behalf of the Noticee on the stipulated hearing dates i.e on September 28, 2016 and on January 18, 2019 and during the course of hearing, the authorized representatives reiterated the submissions made by the Noticee vide its earlier letters, details of which have already been discussed

above. Further, the Noticee also made the following additional submissions vide its letter dated October 13, 2016 and the relevant excerpts from the said letter dated October 13, 2016 are as follows:--

a) *The F & O series wise summary for our Company for relevant days of impugned transactions i.e. for 23.03.2005 and 24.03.2005 is furnished in 'Annexure 1* and 'Annexure 2' respectively to present reply.*

b) *From aforementioned Table 1 to 5, it is can be clearly observed that that impugned transaction of 132.94 lacs was miniscule percentage of our total volume in the market at relevant point of time. Further, from Annexure 1 & 2 it can be observed that we had traded in many future and option contracts at relevant point of time. We submit that on meagre turnover of impugned trades in comparison to our total volume, adverse inferences are drawn against us in SCN and erroneously present proceedings is re-initiated against us.*

c) *On perusal of Annexure B to SCN, we understand that 40 trades were carried out in 16 different unique client codes [15 clients and 1 pro-account]. It is pertinent to note that clients have traded in single contract of buying and selling i.e. squared up contract on same day.*

d) *Further, we submit that unlike earlier outcry system of trading, in today's world, trading is carried out through the online anonymous mechanism of exchange and it is not possible for anyone to know the counter party broker or clients. At broker level, we can set only respective limits of trading for clients. It is next to impossible for TM to monitor each and every underlying stock and strike price at which it is executed.*

e) *The impugned transactions were carried out in future and option segment of NSE Ltd and thus by its very nature there is no transfer of beneficial ownership in such securities. Therefore, alleged violation that our transactions were no intended to effect beneficial ownership is misdirected since transactions in F/O segment are not meant for taking delivery. Further, none of impugned transactions were intended to*

operate as device to inflate, depress or cause fluctuations in price of any security for any wrongful gain or avoidance of loss. In fact, it is mentioned in investigation report itself that "...According to the exchange, no major variation in the underlying price. As can be seen from table given below, the total traded quantity in option segment is insignificant in comparison to market volume in cash segment of respective scrip..." [Internal Page 8 of Investigation Report]. Thus, we submit that alleged violation of Regulations 4 (2) (b) of PFUTP Regulations is not applicable in our case and we deny violation of the same.

CONSIDERATION OF ISSUES AND FINDINGS

11. I have carefully perused the documents/material available on record, the various submissions made by the Noticee (both oral and written) in the said matter and also the facts and circumstances of the case. It is alleged that Noticee has indulged in reversal transactions in the F & O segment of NSE with its counter parties/clients, which were non-genuine transactions and such transactions were executed by the Noticee in collusion with its clients and trading members. It was therefore alleged that Noticee has violated the provisions of Regulations 4(1), 4(2)(a), 4(2)(b), 4(2)(e), 4(2)(g) and 4(2)(n) of PFUTP Regulations and also the provisions of Clauses A(1), A(2), A(3), A(4) and A(5) of the Code of Conduct prescribed for Stock Brokers contained in Schedule II to Regulation 7 of the Stock Broker Regulations**.**

12. In the context of the present matter, it is pertinent to mention that in another case relating to irregularities observed in the F&O trading at NSE, similar allegations were levelled against several entities/stock brokers (including the Noticee) in the matter of executing reversal transactions / non-genuine transactions in collusion with the counter party clients and stock brokers during the period January-March 2007. In the above said matter, the Whole Time Member SEBI through his Order dated June 18, 2007 had issued directions to several entities/stock brokers

(including the Noticee) under the provisions of sections 11B and 11D of the SEBI Act wherein directions were issued to the entities/brokers (including the Noticee) to cease and desist from indulging in such irregular transactions, which were in violation of the provisions of PFUTP Regulations and the Code of Conduct prescribed for stock brokers contained in the Stock Broker Regulations.

13. In the same matter, it was observed that adjudication proceedings were also separately initiated by SEBI against the entities/stock brokers (including the Noticee). However, Noticee settled the adjudication proceeding initiated against it through consent mechanism and the said proceeding was settled by the Noticee vide Settlement Order dated November 10, 2008 on settlement terms of Rs. 4,00,000/- .

14. Meanwhile, Whole Time Member- SEBI vide his Order dated June 18, 2007 had observed that the entities/brokers have indulged in non-genuine trades in the options segment which appeared to be synchronized in nature and one of the parties to the transaction had a positive close out difference whereas, the other party to the transaction had a negative close out difference. Similar views were also expressed by the Adjudicating Officers of SEBI in their respective adjudication orders that were passed against the persons/entities who had indulged in such transactions. In the above mentioned enforcement orders, it was observed by the competent authorities that such transactions and their close-out transactions were executed in various options contracts on different underlying with no or small outstanding open interest position and the first and the reversal/close out transactions were executed at significantly varying prices within a short period of time. Aggrieved by the Order of Whole Time Member- SEBI and also the adjudication orders passed by the AOs of SEBI in the above said matter, some of the entities preferred an appeal against the said orders before the Hon'ble SAT. Hon'ble SAT, vide its orders dated October 11, 2010, October 26, 2010 and November 16, 2010 set-aside the aforementioned Order dated June 18, 2007 passed by Whole Time Member, SEBI and also set aside the Adjudication Orders passed by the AOs against various entities in similar matters pertaining to

the reversal trades and non-genuine transactions executed by the entities in the option segment of NSE. Aggrieved by the Orders passed by Hon'ble SAT in the matter, SEBI preferred an appeal before the Hon'ble Supreme Court of India under the provisions of section 15Z of the SEBI Act. The Hon'ble Supreme Court of India in the matter of *Securities and Exchange Board of India vs. Rakhi Trading Private Limited* (Civil Appeal Nos. 1969, 3174-3177 and 3180 of 2011 dated February 08, 2018) set aside the SAT Orders dated October 11, 2010, October 26, 2010 and November 16, 2010 and upheld the PFUTP charges/allegations levelled against the traders/entities/clients by SEBI and concluded that such transactions executed by the entities in the options segment were non-genuine transactions and were executed with manipulative intent.

15. In the context of the present matter and before dealing with the aforesaid charges in seriatim, the relevant legal provisions of law, the contraventions of which have been alleged in this case against the Noticee are mentioned as under:

PFUTP Regulations

4. Prohibition of manipulative, fraudulent and unfair trade practice

(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;

Broker Regulations

7. *The stock-broker holding a certificate shall at all times abide by the Code of Conduct as specified at 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.*

(3). *Manipulation: A stock-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.*

(4). *Malpractices: A stock-broker shall not create false market either singly or in concert with others or indulge in any act detrimental to the investors' interest or which leads to interference with the fair and smooth functioning of the market. A stock-broker shall not involve himself in excessive speculative business in the market beyond reasonable levels not commensurate with his financial soundness.*

(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."*

16. In the instant matter, I find that the SCN has alleged that the Noticee has executed 40 non-genuine trades / reversal trades during the above mentioned investigation period. In all these trades, Noticee was either the buyer or seller through its proprietary/own trading account and the counterparties to the transactions were the clients of the Noticee. There were 15 such clients with whom Noticee had indulged in such trades by acting as a counter party. The Noticee has contended that these transactions with a total turnover of Rs. 1.33 Crore was miniscule when compared to its total trading turnover of around Rs. 3 lakh crore, which was registered during the aforementioned investigation period. Further, the Noticee mentioned that its overall turnover in the option segment of NSE during the investigation period was more than Rs. 8,000 crore. I observe from the SCN and

the Investigation report that the close-out difference w.r.t these transactions undertaken by the Noticee during the investigation period was Rs 40.23 lacs. I also find from the examination of the trade/order logs pertaining to these transactions that Noticee has consistently taken loss into its books by acting as a counter party to the 15 clients and by trading in its own/proprietary account. In other words, the Noticee, by trading in its proprietary account, either on the buy side or on the sell side, facilitated its clients by executing these transactions. In its reply to the SCN, the Noticee has contended that the close-out difference pertaining to the trades of its clients, as mentioned above, cannot be considered as significant amount for a period of two months i.e. February and March 2005, with 41 working days.

17. Reversal trades are considered as those trades in which an entity reverses it's buy or sell position in a contract with subsequent sell or buy positions with the same counterparty during the same day. The said reversal trades are alleged to be non-genuine trades as they are not executed in the normal course of trading, lack basic trading rationale, and allegedly lead to false or misleading appearance of trading, hence, these trades are deceptive and manipulative in nature and are non-genuine trades. Such deceptive trades can also cause artificial volume in the security and has the potential to distort the market equilibrium. From the facts/material made available, I find that the repeated reversal trades executed by the Noticee in its proprietary account with its clients (15 clients), which was observed in the present case, were undertaken by the Noticee, with a pre-determined arrangement to book profit or losses respectively, and therefore, the parties to the trades (including the Noticee) were not trading in the normal sense and ordinary course of business. It is therefore alleged that the Noticee by indulging in reversal trades with its clients and by acting as a counterparty to such trades in the illiquid stock option segment at NSE has managed to generate misleading appearance of trading without any change of beneficial ownership, in the Stock Options segment at NSE during the investigation period.

18. The summary of the trades executed by the Noticee in the options segment of NSE during the investigation period is mentioned in the Table as under:-

Members Name	***No. of clients***	***Gross Traded Value (in Rs. lakh) of trades done***	***Gross Traded Value (in Rs. lakh) of trades done for clients***	***Gross Traded Value (in Rs. lakh) of trades done in proprietary account***
Shilpa Stock Brokers Pvt Ltd	*15 clients*	*132.94*	*132.94*	*132.94*

Thus, I observe from the above that all the non-genuine/reversal trades were executed by the Noticee in its proprietary account and for and on behalf of its 15 clients wherein the Noticee was either the buyer or seller in respect of these trades. The Noticee has acted as a counterparty to such non-genuine trades on behalf of its clients and have taken loss into its books as a result of such trades.

19. In this regard, it is pertinently noted upon examination of the trade log of the Noticee that it had executed 40 reversal/ non-genuine trades in 6 contracts and Noticee consistently took loss into its books as a result of the 40 reversal trades with its clients. I further observe from the trades executed by the Noticee that it has also resulted in the creation of artificial turnover of approximately Rs 1.33 crore in the given 6 contracts and the said trades have also resulted in a negative close out difference of approximately Rs. 40.23 lakh as the Noticee consistently took loss into its books as a result of such collusive trades with its counter parties. It is further noted that these trades were also reversed / squared up within a short span of time with the same counterparty i.e. the trades were reversed within seconds on many days. Thus, it is observed that Noticee had indulged in reversal trades with its counterparties in the stock option segment of NSE and the same has clearly resulted in non-genuine trades.

20. To illustrate, it is observed that the Noticee had executed 2 trades on March 24, 2015 in the contract of Call Option of BHEL expiring on March 31, 2005. It is observed that the Noticee, at 14:09:12 on March 24, 2005 purchased 2,400 units

of the aforesaid options at a price of Rs. 48 from its client Mundra Polytex. The Noticee purchased it from Mundra Polytex in its own/proprietary account This buy trade of the Noticee was immediately followed by sell trade made by the Noticee, at 14:10:22, of the same option of 2,400 units at Rs. 15 with Mundra Polytex i.e within 1 minute of the buy trade i.e the Noticee was the seller and Mundra Polytex was the buyer. This resulted in trades with total traded quantity of 4800 units and negative close out difference of Rs. 79,200, which was taken into the books of the Noticee. Thus, apart from abnormal difference between the prices at which the trades were executed without corresponding effect on the price of underlying security, the above trade also caused artificial volume to the tune of 4800 units as a result of such reversal trades. The trade log examined during the investigation period shows that Noticee had indulged in many transactions of such kind and had taken loss into its books. Clearly, in my opinion, these trades were non-genuine and were against the transparent principles of trades in the stock market.

21. The Noticee has vehemently contended that there is complete anonymity in a screen based trading system and that the details of the counterparty to the trades were not known to the Noticee. However, considering the precision at which the reversal transactions had taken place, the quantity, price, time and sale, parties being persistent in a large number of such trade transactions with huge price variations, I am of the view that it will be too naïve to hold that these transactions are through screen-based trading and hence anonymous. Such conclusion would be over-looking the prior meeting of minds involving synchronization of buy and sell order w.r.t the transactions entered into by the Noticee with its counterparties (which are its own clients) and such synchronized trading is clearly violative of the transparent norms of trading in the securities market. In view of the above observations, I hold that all the 40 transactions executed by the Noticee in the 6 Options Contracts were synchronized trades, which were reversed within a small time gap and with prior meeting of mind with its clients. Needless to mention the fact that these transactions were manipulative/deceptive device with a view to create a desired loss and/or profit in the books of the parties to the said

transactions and in the process, artificial volumes were also generated through such non-genuine trades.

22. At this juncture, it is pertinent to refer to the observations made by Hon'ble Supreme Court of India in the matter of *Securities and Exchange Board of India vs. Rakhi Trading Private Limited* (Civil Appeal Nos. 1969, 3174-3177 and 3180 of 2011 dated February 08, 2018) wherein, the Hon'ble Supreme Court while cumulatively analyzing the reversal transactions held that, "*From the facts before us, it is clear that the traders in question did not intend to transfer beneficial ownership and therefore these trades are non-genuine. Rather than allowing the market forces to operate in their natural course, the traders repeatedly carried out the impugned transactions which deprived other market players from full participation. The repeated reversals and predetermined arrangement to book profits and losses respectively, made it clear that the parties were not trading in the normal sense and ordinary course. Resultantly, there has clearly been a restriction on the free and fair operation of the market forces in the instant case"*

23. In the same matter, Hon'ble Supreme Court further made the following observations :-

"……..quantity, time and significant variation of prices, without major variation in the underlying price of the securities clearly indicate that Respondent's trades are not genuine and had only misleading appearance of trading in the securities market……...".

"35…Contextually and in simple words, it means a practice which does not conform to the fair and transparent principles of trades in the stock market. In the instant case, one party booked gains and the other party booked a loss. Nobody intentionally trades for loss. An intentional trading for loss per se, is not a genuine dealing in securities. The platform of the stock exchange has been used for a non-genuine trade. Trading is always with the aim to make profits. But if one party

consistently makes loss and that too in preplanned and rapid reverse trades, it is not genuine…….

36. ……Ordinarily, the trading would have taken place between anonymous parties and the price would have been determined by the market forces of demand and supply. In the instant case, the parties did not stop at synchronised trading. The facts go beyond that. The trade reversals in this case indicate that the parties did not intend to transfer beneficial ownership and through these orchestrated transactions, the intention of which was not regular trading, other investors have been excluded from participating in these trades. The fact that when the trade was not synchronizing, the traders placed it at unattractive prices is also a strong indication that the traders intended to play with the market….

"37. …No doubt, as in the case of trade in a scrip in the cash segment, there is no physical delivery of the asset. However, even in the derivative segment there is a change of rights in a contract. In the instant case, through reverse trades, there was no genuine change of rights in the contract"

24. In this context, I also find it relevant to refer to the decision of Hon'ble Supreme Court in the matter of *Securities and Exchange Board of India v. Kishore R Ajmera {(2016)} 6 SCC 368 : AIR 2016 SC 1079} wherein, the Hon'ble Supreme Court has held*, " …….. *According to us, knowledge of who the 2nd party/client or the broker is, is not relevant at all. While the screen based trading system keeps the identity of the parties anonymous it will be too naïve to rest the final conclusions on the said basis which overlooks a meeting of minds elsewhere. Direct proof of such meeting of minds elsewhere would rarely be forthcoming. The test, in our considered view, is one of preponderance of probabilities so far as adjudication of civil liability arising out of violation of the Act or the provisions of the Regulations framed thereunder is concerned……..."*

25. In the same matter, Hon'ble Supreme Court has further held that, "…….. *In the absence of direct proof of meeting of minds elsewhere in synchronized*

transactions, the test should be one of preponderance of probabilities as far as adjudication of civil liability arising out of the violation of the Act or provision of the Regulations is concerned. The conclusion has to be gathered from various circumstances like that volume of trade effected; the period of persistence in trading in a particular scrip; the particulars of buy and sell orders, namely the volume thereof; the proximity of time between the two and such relevant factors…."

26. The observations made in the aforesaid judgments of Hon'ble Supreme Court apply with full force to the facts and circumstances of the present case. Therefore, applying the ratio of the above judgments, I am convinced that the execution of trades by the Noticee in the illiquid options segment with such precision in terms of order placement, time, price, quantity etc. and also the fact that the transactions were reversed consistently with the same counterparties indicates a prior meeting of mind with a view to execute the reversal trades at a pre-determined price. Since these trades were done in the illiquid option contracts (as the strike price was far away from the market price of the underlying), there was no price discovery. The only reason for the wide variation in prices of the same contract, within seconds/minutes was a clear indication that there was pre-determination in the prices by both the counterparties when executing the trades. Thus, the nature of trading, as brought out above, clearly indicates an element of prior meeting of minds and therefore, a collusion of the Noticee with its counterparties to carry out the trades at pre-determined prices. It is not possible to comprehend the reason for which the Noticee would enter into an option contract with a strike price very far away from the current market price of the underlying except for the fact that it wanted to execute non-genuine trades. One also cannot comprehend to the fact that the Noticee was consistently taking loss into its books as a result of such trades. The various contentions ascribed by the Noticee such as, the impugned trades were carried out in the F & O segment and thus by its very nature there can be no transfer of beneficial ownership of the securities, that at the stock broker level it was impossible for the Noticee to monitor the activities of its clients etc are

weak arguments as the records prove that Noticee was a direct party to these transactions by trading in its proprietary account (either on the buy side or sell side) and the trades were reversed by the Noticee with its counter parties i.e 15 clients with such precision in terms of quantity, time, rate etc on a consistent basis. Further, the factual position w.r.t the other contention of the Noticee that the impugned trades were carried out by it in the F & O segment and thus by its very nature there can be no transfer of beneficial ownership of the securities is also without any merit as these issues have been adequately addressed by Hon'ble Supreme Court of India in the matter of *Securities and Exchange Board of India v. Rakhi Trading Private Limited* (Civil Appeal Nos. 1969, 3174-3177 and 3180 of 2011 dated February 08, 2018). In view of the same, I am not inclined to make any further observations in the matter.

27. Rather than allowing the market forces to operate in their natural course, the Noticee repeatedly carried out the impugned transactions with its counterparties which deprived other market players from full participation. The repeated reversals and pre-determined arrangement to book profits and losses respectively, made it clear that the parties, including the Noticee, were not trading in the normal sense and ordinary course of business. Resultantly, there has clearly been a restriction on the free and fair operation of market forces in the instant case. Such trading also involves an act amounting to manipulation of the price of the security in the sense that the price has been artificially and apparently prefixed. The price does not at all reflect the value of the underlying asset. It is also a transaction without any intention of performing it and without any intention of effecting a change of ownership of such securities, ownership being understood in the limited sense of the rights in the contract. By synchronization and repeated reversal trades, as has been carried out by the Noticee in the instant matter, the price discovery system itself is affected. Except the parties who have pre-fixed the price, nobody is in the position to participate in the trade. It also has an adverse impact on the fairness, integrity, and transparency of the stock market.

28. In the instant case, it is clearly established that the Noticee has aided and abetted its clients in entering into non-genuine trades because for every trade executed by the Noticee for its clients, Noticee has acted as counter party to such trades through its proprietary account. Therefore, in my opinion, there is direct evidence of collusion of the Noticee with its clients' w.r.t the above mentioned trades. As a stock broker, the Noticee was expected to play the role of a gatekeeper and not place the trades in a mechanical manner with ulterior intentions. The instant case goes beyond the realm of lack of due diligence and care exercised by the Noticee, and quite clearly, it is an act whereby Noticee has aided and abetted its clients in the commission of the manipulative/non-genuine trades. In view of the aforesaid failure on the part of the of the Noticee and the manner in which Noticee has carried out the above trades, I am convinced that Noticee has violated the provisions of Regulations 4(1) and 4(2) (a) of the PFUTP Regulations and also the provisions of Clauses A(1) to A (5) of the Code of Conduct prescribed for Stock Brokers contained Schedule II to Regulation 7 of the Stock Broker Regulations.

29. In view of the above observations, I conclude that the Noticee is liable for monetary penalty under the provisions of sections 15HA and 15HB of the SEBI Act, which reads as under :

> ***Penalty for fraudulent and unfair trade practices.***
>
> ***15HA.*** *If any person indulges in fraudulent and unfair trade practices relating to securities, he shall be liable to a penalty which shall not be less than five lakh rupees but which may extend to twenty-five crore rupees or three times the amount of profits made out of such practices, whichever is higher.*
>
> ***15HB.*** *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.*

30. In this regard, the provisions of Section 15J of the SEBI Act and Rule 5 of the Adjudication Rules require that while adjudging the quantum of penalty, 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.

31. Clearly, from the above observations, the Noticee was instrumental in executing the reversal/non-genuine transactions in the illiquid options contracts segment of NSE during the investigation period by consistently executing these transactions in its proprietary account for and on behalf of its and its clients. As a stock broker, Noticee through its proprietary account was seen either on the buy side or sell side of the transactions entered into with its counterparties and in this manner, Noticee has colluded with its clients. In the process, Noticee was also responsible for generating artificial volumes in such illiquid contracts through such non-genuine trades at NSE. It is on record that the Noticee has entered into 40 non-genuine transactions in 6 stock option contracts with its 15 clients as counterparties which clearly demonstrates the repetitive nature of the default on the part of the Noticee. The Noticee, as a responsible stock broker in the securities market, was expected to perform with high standards of integrity and fairness and comply with the relevant provisions of law at all times. However, Noticee not only acted in a fraudulent manner by indulging in non-genuine transactions but also failed in its duties and obligations as a stock broker by aiding and abetting its clients in executing these transactions. From the manner in which Noticee executed the above mentioned transactions, the Noticee has violated the statutory provisions of law. In this context, reliance is placed upon the order of the Hon'ble Supreme Court of India in the matter of Chairman, SEBI Vs Shriram Mutual Fund {[2006]5 SCC 361} – wherein the Hon'ble Supreme Court of India

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……...*"

ORDER:

32. Having considered all the facts and circumstances of the case, the material available on record and the factors mentioned in the preceding paragraphs, I, in exercise of the powers conferred upon me under Section 15-I of the SEBI Act read with Rule 5 of the Adjudication Rules, hereby impose a total penalty of Rs 20,00,000/- on the Noticee viz. M/s Shilpa Stock Brokers Pvt Ltd under the provisions of sections 15HA and 15HB of the SEBI Act, details of which are as under:

Name of the Noticee	**Violations of the provisions of law**	**Sections under which penalty is imposed**	**Penalty (Rs.)**
M/s Shilpa Stock Brokers Pvt Ltd	Regulations 4(1) and 4(2)(a) of PFUTP Regulations	Section 15HA of the SEBI Act	10,00,000/- (Rs. Ten lakhs)
	Clauses A(1), A(2), A(3), A(4) and A(5) of the Code of Conduct prescribed for Stock Brokers contained in Schedule II to Regulation 7 of	Section 15HB of the SEBI Act	10,00,000/- (Rs. Ten lakhs)

	the Stock Broker Regulations		
Total penalty amount			**Rs.20,00,000/- (Rs. Twenty lakhs)**

33. The Noticee shall remit / pay the said amount of penalty within 45 days of the receipt of this order either by way of Demand Draft in favour of "SEBI - Penalties Remittable to Government of India", payable at Mumbai, OR through e-payment facility into the Bank Account, the details of which are given below:-

Account No. for remittance of penalties levied by Adjudication Officer	
Bank Name	State Bank of India
Branch	Bandra-Kurla Complex
RTGS Code	SBIN0004380
Beneficiary Name	SEBI – Penalties Remittable To Government of India
Beneficiary A/c No	31465271959

34. The Noticee shall forward the said Demand Draft or the details / confirmation of penalty so paid through e-payment to the Division Chief of Division of Regulatory Action-4, Enforcement Department-1 (EFD1-DRA4) of SEBI. The format for forwarding details / confirmation of the e-payments made to SEBI shall be in the form as provided at Annexure A of Press Release No. 131/2016 dated August 09, 2016 shown at the SEBI Website which is mentioned as under:

1. Case Name:	
2. Name of Payee:	
3. Date of payment:	

4. Amount Paid:	
5.Transaction No:	
6. Bank Details in which payment is made:	
7. Payment is made for: (like penalties /disgorgement/recovery/Settlement amount and legal charges along with order details)	

35. In terms of the provisions of Rule 6 of the Adjudication Rules, a copy of this order is sent to the Noticee viz. M/s Shilpa Stock Brokers Pvt Ltd. and also to Securities and Exchange Board of India.

Place: Mumbai **SURESH B. MENON**
Date: February 28, 2019 **ADJUDICATING OFFICER**