

**BEFORE THE ADJUDICATING OFFICER
SECURITIES AND EXCHANGE BOARD OF INDIA
[ADJUDICATION ORDER NO. Order/PM/AB/2019-20/6693]**

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

In respect of:
Ms. Mamta Jain
PAN: AAPPJ6257K

In the matter of *Dealing in Illiquid Stock Options at the BSE*

FACTS OF THE CASE

1. Securities and Exchange Board of India (hereinafter be referred to as, the “**SEBI**”) conducted investigation into the trading activity in illiquid stock options on BSE Limited (hereinafter be referred to as, the “**BSE**”) for the period April 01, 2014 to September 30, 2015 (hereinafter be referred to as, the “**Investigation Period**”) after observing large scale reversal of trades in the Stock Options segment of the BSE.
2. Investigation revealed that during the Investigation Period, a total of 2,91,643 trades comprising 81.38% of all the trades executed in the BSE Stock Options Segment were trades which involved reversal of buy and sell positions by the clients and counterparties in a contract. Ms. Mamta Jain (hereinafter be referred to as, the “**Noticee**”) was one such client whose reversal trades involved squaring off open positions with a significant difference without any basis for such change in the contract price. The aforesaid reversal trades allegedly resulted into generation of artificial volumes, leading to allegations that the Noticee had violated Regulation 3(a), (b), (c), (d) and Regulation 4(1), 4(2) (a) of the SEBI (Prohibition of Fraudulent and Unfair Trading Practices related to

Securities Markets) Regulations, 2003 (hereinafter be referred to as, the “**PFUTP Regulations**”).

APPOINTMENT OF ADJUDICATING OFFICER

3. SEBI initiated adjudication proceedings and appointed the undersigned as Adjudicating Officer under Section 15-I of the Securities and Exchange Board of India Act, 1992 (hereinafter be referred to as, the “**SEBI Act**”) read with Rule 3 of the SEBI (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules, 1995 (hereinafter be referred to as, the “**Adjudication Rules**”) *vide* order dated April 3, 2018 to inquire into and adjudge under Section 15HA of the SEBI Act against the Noticee for the alleged violation of aforesaid provisions of PFUTP Regulations. The appointment of the AO was communicated *vide* order dated May 29, 2018.

SHOW CAUSE NOTICE, REPLY AND HEARING

4. A Show Cause Notice dated September 27, 2018 (hereinafter be referred to as, the “**SCN**”) was served upon the Noticee under Rule 4(1) of the Adjudication Rules to show cause as to why an inquiry should not be held and penalty be not imposed against it under Section 15HA of the SEBI Act for alleged violations of Regulations 3(a),(b),(c),(d) and 4(1), 4(2)(a) of the PFUTP Regulations.
5. The allegations levelled against the Noticee in the SCN are summarized as below:
 - a) That the Noticee was one of the entities which indulged in reversal trades which allegedly created false and misleading appearance of trading, generating artificial volumes in Stock Options segment of the BSE during the Investigation Period.
 - b) That the Noticee engaged in 76 instances in 11 unique contracts which led to generation of artificial volume in these unique contracts.
 - c) The trades entered by the Noticee were reversed on the same day with same counterparties at a substantial price difference without any basis for significant change in the contract price which indicates that these trades are artificial and are non-genuine in nature.

- d) A summary of dealings of the Noticee in the 11 Stock Options contracts in which the Noticee executed non-genuine reversal trades during the Investigation Period are as under:

Table 1: Summary of trading of the Noticee in Illiquid Stock Options on BSE

S. No.	Contract Name	Avg. Buy Rate (Rs.)	Total Buy Volume (no. of units)	Avg. Sell Rate (Rs.)	Total Sell Volume (no. of units)	% of Artificial trades of the Noticee in the contract to Total trades in the contract	% of Artificial Volume generated by Noticee in the contract to Total Volume in the Contract
1	ADEL15MAR680.00CEW1	22.66	101000	48.59	101000	9%	8%
2	ALBK15FEB95.00CEW3	8.40	26000	15.49	26000	29%	13%
3	AMBC15FEB245.00CE	12.20	99000	22.09	99000	39%	35%
4	AMBC15MAR250.00CEW1	21.10	252000	34.80	252000	35%	58%
5	APLT15MAR160.00CEW1	12.20	110000	22.96	110000	100%	100%
6	APLT15MAR165.00CEW1	13.10	76000	20.80	76000	33%	23%
7	ARVI15MAR290.00CEW1	11.30	221000	21.15	221000	19%	56%
8	BHEL15MAR290.00PEW1	12.86	115000	26.10	115000	83%	88%
9	COAL15FEB370.00CE	11.19	151000	22.20	151000	43%	33%
10	DLFL15FEB135.00CE	9.40	152000	19.33	152000	30%	30%
11	HNZL15APR140.00CEW1	24.60	218000	13.40	218000	50%	56%

- e) By indulging in execution of aforesaid non-genuine reversal trades, the Noticee has violated Regulations 3(a),(b),(c),(d) and 4(1), 4(2)(a) of the PFUTP Regulations, text of which is reproduced as under:

“SEBI (Prohibition of Fraudulent and Unfair Trading Practices Related to Securities Markets) Regulations, 2003

3. Prohibition of certain dealings in securities

No person shall directly or indirectly -

- (a) buy, sell or otherwise deal in securities in a fraudulent manner;*
- (b) use or employ, in connection with issue, purchase or sale of any security listed or proposed to be listed in a recognized stock exchange, any manipulative or deceptive device or contrivance in contravention of the provisions of the Act or the rules or the regulations made thereunder;*
- (c) employ any device, scheme or artifice to defraud in connection with dealing in or issue of securities which are listed or proposed to be listed on a recognized stock exchange;*
- (d) engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person in connection with any dealing in or issue of securities which are listed or proposed to be listed on a recognized stock exchange in contravention of the provisions of the Act or the rules and the regulations made there under.*

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 or 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;

.....”

6. The SCN was sent to the Noticee by way of Speed Post with Acknowledgment Due (hereinafter be referred to as, the “SPAD”). However, no reply was received in response to the SCN.

7. After considering the facts and circumstances of the case, the undersigned granted an opportunity of personal hearing to the Noticee on October 22, 2019 *vide* Notice of Hearing dated October 07, 2019. The hearing notice was sent by SPAD and by e-mail. The hearing notice was duly delivered through both the means. The Noticee subsequently sent an email on October 15, 2019 seeking an adjournment due to festival. In response to said e-mail, the Noticee was intimated by e-mail dated October 17, 2019 that the next date of hearing was fixed on November 6, 2019. *Vide* email dated October 26, 2019 the Advocate for the Noticee sought certain documents which were provided on October 29. On November 6, 2019 the Advocate for the Noticee *vide* its emails sought an adjournment and requested that hearing should be fixed on November 19 or 21. Considering the said request the hearing was fixed on November 19, 2019. On the said date the Advocates of Noticee attended the hearing and during the course of hearing submitted a reply to SCN.
8. The submissions of the Noticee are summarized as under:
- a) The matter suffers from delay as the transactions took place in 2015 but SCN was issued only in 2018.
 - b) No alert for the trading was raised by the BSE and the alleged reversal trades constituted only 0.026% of the total reversal trades.
 - c) No nexus has been established between the Noticee and the counterparties and in absence of any nexus the trading cannot be called artificial.
 - d) The trading done is intra-day and in order to avoid overnight risks the positions have to be settled. Further, intra day trading is permissible and not illegal.
 - e) The volume done by the Noticee cannot be called non-genuine as no one considered it to be non-genuine and even BSE did not annul the trading of the Noticee.
 - f) On account of illiquidity in the options market there were differences in in option premium and such differences were a market feature. However, the rate difference were within the limits and were anonymously matched.

- g) All the trading done by the Noticee was genuine, bonafide and in normal course of business without any fraudulent/manipulative intent.
- h) Reliance has been placed on the order of Hon'ble SAT in the matter of ***Kapil Chaturabhuj Bhuptani v. SEBI***, (Order dated October 10, 2013) and ***Shri Nagad Sarvar v. SEBI*** (Order dated August 6, 2019).

CONSIDERATION OF ISSUES AND FINDINGS

9. The issues that arise for consideration in the instant matter are:

Issue No. I Whether the trading in illiquid Stock Options done by the Noticee during the Investigation Period were in violation of Regulations 3(a), (b), (c), (d) and 4(1) & 4(2)(a) of the PFUTP Regulations?

Issue No. II If yes, whether the violation, on the part of the Noticee would attract monetary penalty under Section 15HA of the SEBI Act?

Issue No. III If yes, what would be the monetary penalty that can be imposed upon the Noticee taking into consideration the factors stipulated in Section 15J of the SEBI Act read with Rule 5 (2) of the Adjudication Rules?

Issue No. I **Whether the trading in illiquid Stock Options done by the Noticee during the Investigation Period were in violation of Regulations 3(a), (b), (c), (d) and 4(1) & 4(2)(a) of the PFUTP Regulations?**

10. As stated in preceding paragraphs, the position /trades entered into by the Noticee were squared up within a short span. The striking feature of the trades of the Noticee was that all the positions/trades were squared with the same counterparty with whom Noticee had originally traded/created position. The squaring up of the position/trade was at the substantial variation of price from the original position/trade. Thus, it was alleged that the Noticee had indulged in reversal trades. The said allegation was supported with evidence from the trade log containing records of all trades and reversal trades carried out by the Noticee in the Stock Options segment of the BSE during the Investigation Period and was also provided to the Noticee along with the SCN. On perusal of the details of trades carried out by the Noticee, it is observed that the Noticee

took positions and then squared it up in 76 instances in 11 unique option contracts during the Investigation Period.

11. To illustrate, on February 28, 2015, the Noticee bought 1,10,000 units of the contract APLT15MAR160.00CEW1 at 10:40:12 (Buy order placed at 10:40:12; Sell Order placed at 10:40:11) from SHPL Enterprise at a price of Rs. 12.20. Thereafter, the Noticee reversed its position by selling 1,10,000 units in 6 different trades to the same counterparty between 10:40:16 – 10:40:50 (Buy orders placed between 10:40:16 – 10:40:50; Sell Orders placed between 10:40:16 – 10:40:50) at an average price of Rs. 22.96. Thus, the position of the Noticee was squared up at an average difference of Rs. 10.76. The entire volume of 2,20,000 units in the said option contract was arising out of the trades done by the Noticee.
12. A similar *modus operandi* is seen to be adopted by the Noticee in its trades in the other 10 unique option contracts. It is observed from the trading of the Noticee that in all the trades of the Noticee the buy order and sell order has been entered in less than a second of each other. As stated earlier, there is a substantial variation in price in both the legs.
13. From the reply of the Noticee, I note that the Noticee has not disputed execution and subsequent reversal of trades as alleged in the SCN. However, the Noticee, in her reply, has contended that the transactions were carried out by her at an anonymous platform provided by the BSE. The Noticee has also contended that there is nothing in SCN to show that she has violated any law and that intra day reversal was legal. I have considered the aforementioned contentions of the Noticee. In this regard, it may be noted that the Noticee was given details of its trades in the BSE options segment and the details of the trades which are alleged to be reversed and manipulative. The material provided to the Noticee is sufficient to level allegation of artificial volume creation on the Noticee. Further, I find it relevant to refer to the decision of the 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 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....”

14. The 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 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...”. Placing reliance of the observation of the Hon’ble Supreme Court in the aforementioned matter, I cannot accept the submission of the Noticee that transactions were genuine on account of them being carried out on an anonymous platform of the exchange wherein, the Noticee had no knowledge of the counterparty. The manner of placement of the orders in both legs signify that the orders were entered in a premeditated manner and were not genuine in any manner.

15. At this juncture, I also find it relevant to refer to the decision of the Supreme Court 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) wherein, the Hon’ble Supreme Court while cumulatively analyzing the reversal transactions held that, “Considering the reversal transactions, quantity, price and time and sale, parties being persistent in number of such trade transactions with huge price variations, it will be too naïve to hold that the 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 and not negotiated deals as per the board's circular. The impugned transactions are manipulative/deceptive device to create a desired loss and/or profit. Such

synchronized trading is violative of transparent norms of trading in securities”
The Court further stated that “.....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 hand only misleading appearance of trading in the securities market.....”.

16. Applying the ratio of the Supreme Court in the matter of **Kishore R. Ajmera** (*supra*) and **Rakhi Trading** (*supra*), I am of the view that execution of trades in an illiquid market with such precision in order placement indicates a prior meeting of mind with a view to execute the reversal trades at a pre-determined price. The Noticee has failed in explaining the rationale for the trading as mentioned in Table 1 wherein it has taken a position at a particular price and squared it up at significant price difference without any substantial variation in the price of underlying. Since, the option contracts were done in illiquid contracts (as the strike price was far away from the market price of underlying), there was no trading in the said contract and hence no price discovery. The only reason for the wide variation in prices of the same contract, within minutes and some, even seconds, was pre-determination in the prices by both 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 to carry out 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.
17. The Noticee has referred to the judgment of **Shri Nagad Sarvar** (*Supra*) in its submission. On perusal of the said judgement it is observed that one of the crucial factors considered by the Hon’ble SAT in the aforesaid order was time interval in which the buy order and sell orders were placed. In the aforesaid case the interval in placement of orders was substantial but in the case of the Noticee, there was almost no time gap in placement of orders. Thus, the reliance of the Noticee on the aforesaid order is misplaced and it can be inferred that the Hon’ble SAT would have opined otherwise if the time gap in placement of orders was negligible.

18. Further, it is observed from Table 1 above that the Noticee, on an average contributed 45.52% of the volume in the 11 contracts, wherein the Noticee has contributed 50% or more volume in 5 contracts and more than 20% in another 4 contracts. The high contribution of the trading of Noticee in these contracts show that general public was not interested in such contracts where strike price was far from the market price of underlying. Thus, these contracts were easy to manipulate and were chosen by the Noticee to execute non-genuine trades.
19. I further note that the Supreme Court in the matter of **Rakhi Trading** (*supra*), has held that, “*Regulation 2(1)(c) defines fraud. Under Regulation 2(1)(c)(2) a suggestion as to a fact which is not true while he does not believe it to be true is fraud. Under Regulation 2(1)(c)(7), a deceptive behaviour of one depriving another of informed consent or full participation is fraud. And Under Regulation 2(1)(c)(8), a false statement without any reasonable ground for believing it to be true is also fraud. In a reverse dealing in securities, with predetermined arrangement to book loss or gain between pre-arranged parties, all these vices are attracted.*” I am of the considered view that the scheme, plan, device and artifice employed by the Noticee in this case of executing reversal trades in illiquid stock options contracts at irrational, unrealistic and unreasonable prices, tantamount to fraud on the securities market in as much as it involves non-genuine/ manipulative transactions in securities and misuse of the securities market. The non-genuine and deceptive transactions of the Noticee are, prima-facie, covered under the definition of 'fraud' and the dealings of the Noticee as discussed herein above were “fraudulent”, as defined under regulation 2(1)(c) of the SEBI (PFUTP) Regulations, 2003 and prohibited under the provisions of Regulations 3(a), (b), (c) and (d) and 4(1) and 4(2)(a) SEBI (PFUTP) Regulations, thereof.
20. Considering the synchronized manner of placing buy and sell orders within seconds of each other, reversing of the trades within a short time with widely varying prices of the two legs of trade in the same contract without any basis for such wide variation, I find that the reversal trades executed by the Noticee were *non-genuine* in nature and created an impression of genuine trading volumes in respective contracts. I am of the view that by engaging in such trades, the Noticee has violated provisions of Regulation 4(2)(a) of the PFUTP

Regulations, which states that dealing in securities will be deemed to be a fraudulent or unfair trade practice if it involves “*indulging in an act which creates false or misleading appearance of trading in the securities market*”.

21. I once again find it relevant to place reliance on the decision of the Supreme Court in ***Rakhi Trading*** (*supra*) wherein, the Supreme Court while decision upon a case involving execution of reversal trades in index options, observed, “*the traders thus having engaged in a fraudulent and unfair trade practice while dealing in securities are hence liable to be proceeded against for violation of Regulations 3(a), 4(1) and 4(2)(a) of the PFUTP Regulations.*”

22. In view of the aforesaid, I find that the Noticee, by engaging in such non-genuine transactions, created a misleading impression of trading in respective contracts while dealing in Stock Options contracts in a fraudulent manner. I am of the considered view that the aforesaid act of the Noticee is in clear violation of Regulations 3(a), 4(1) and 4(2) (a) of the PFUTP Regulations.

Issue No. II If yes, whether the violation, on the part of the Noticee would attract monetary penalty under Section 15HA of the SEBI Act?

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Issue No. III If yes, what would be the monetary penalty that can be imposed upon the Noticee taking into consideration the factors stipulated in Section 15J of the SEBI Act read with Rule 5 (2) of the Adjudication Rules?

23. Since violation of Regulations 3(a), 4(1) and 4(2)(a) of the PFUTP Regulations by the Noticee is established, I am of the view that the same warrants imposition of monetary penalty upon the Noticee under Section 15HA of the SEBI Act, text of which is produced as under :

SEBI Act

“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.”

24. While determining the quantum of penalty under Section 15HA of the SEBI Act, the following factors stipulated in Section 15J of the SEBI Act, have to be given due regard:

- 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. As established in the preceding paragraphs, the trades carried out by the Noticee were non-genuine in nature and created a misleading appearance of trading. As brought out earlier, such trades were carried out by the Noticee in illiquid stock options contracts where there was negligible participation by the public. Investigation has shown amount of profit / loss of the counterparties to the trades as a result of such non-genuine trades. However, considering that the violation by the Noticee is creation of artificial trading volumes by trading between two counterparties and wider market is not involved in the trades, the trades are such that one of the counterparty books a profit while the other counterparty books a loss. Hence, it would be appropriate to consider the impact of these transactions between the two counterparties in totality. When the impact of artificial volumes created by the two counterparties is seen as a whole, it is not possible from the material available on record to quantify the amount of disproportionate gain or unfair advantage resulting from the artificial trades between the counterparties or the consequent loss caused to investors as a result of the default.

ORDER

26. After taking into consideration all the facts and circumstances of the case, in exercise of powers conferred upon me under Section 15I (2) of the SEBI Act read with Rule 5 of the Adjudication Rules, I hereby impose a penalty of Rs. 5,00,000/- (Rupees Five Lakhs only) upon the Noticee, under Section 15HA of

the SEBI Act for violation of Regulation 3(a), 4(1) and 4(2)(a) of the PFUTP Regulations.

27. The Noticee shall remit / pay the said amount of penalty within 45 days of receipt of this order either by way of Demand Draft in favour of “SEBI - Penalties Remittable to Government of India”, payable at Mumbai, OR by using the web link <https://siportal.sebi.gov.in/intermediary/AOPaymentGateway.html>
28. The Noticee shall forward said Demand Draft to the Enforcement Department – Division of Regulatory Action – I of SEBI. The Noticee shall provide the following details while forwarding the Demand Draft:
- a) Name and PAN of the entity (Noticee)
 - b) Name of the case / matter
 - c) Purpose of Payment – Payment of penalty under AO proceedings
 - d) Bank Name and Account Number
 - e) Transaction Number
29. Copies of this Adjudication Order are being sent to the Noticee and also to SEBI in terms of Rule 6 of the Adjudication Rules.

Date: January 31, 2020

Place: Mumbai

**PRASANTA MAHAPATRA
ADJUDICATING OFFICER**