BEFORE THE ADJUDICATING OFFICER
SECURITIES AND EXCHANGE BOARD OF INDIA

[ADJUDICATION ORDER/SS/AS/2019-20/3369]

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

In respect of:

Mr. AJAY KUMAR GARG
(PAN: AFIPG4789H)
Shop No 8 561 16,
Chobey Ji Ka Fatak, Kinari Bazar,
Agra - 282001

In the matter of dealing in Illiquid Stock Options at the BSE

1. Securities and Exchange Board of India ('SEBI') observed large scale reversal of trades in the Stock Options Segment of the BSE Limited (hereinafter be referred to as 'BSE') and, pursuant to this, it conducted investigation into the trading activities of certain entities in illiquid Stock Options at the BSE for the period April 01, 2014 to September 30, 2015 (hereinafter be referred to as 'the Investigation Period'). Investigation revealed that during the Investigation Period, a total of 2,91,643 trades (comprising 81.38% of all the trades executed in the Stock Options Segment of BSE) involved reversal of buy and sell positions by the clients and counterparties in a contract. These alleged non genuine trades resulted into creation of artificial volume to the tune of 826.21 crore units or 54.68% of the total market volume in Stock Options segment of BSE during the Investigation Period. It was further noted that said alleged non genuine trades were not restricted to any specific contract or between any specific set of entities.

2. Mr. Ajay Kumar Garg (hereinafter be referred to as 'the Noticee') was one of the several entities which were indulged in execution of such alleged non genuine trades. It was observed from the trade log that the Noticee had executed total 2 reversal trades during Investigation Period in a unique contract -"SUNP15APR1040.00CE" and, in both instances, the trading happened on same day i.e. March 27, 2015. These 2 reversal trades in this unique contracts, allegedly led to generation of artificial volume of 10, 38,000 units of the contract on March 27, 2015. The trades entered by the Noticee were reversed on the same day within 20 minutes with same counterparty 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. A summary of trades of the Noticee in 1 such stock options contracts in which the Noticee allegedly executed non-genuine reversal trades during the Investigation Period is given in the following table:

Table 1: Trades of the Noticee in the contract of "SUNP15APR1040.00CE"

Sl.	Date	Buyer	Seller	Buy Order Time	Sell Order Time	Trade Time	Trade Rate (₹)	Trade Quantity
1	27/03/2015	JAGDISH SINGH	AJAY KUMAR GARG	10:56:54	10:56:54	10:56:54	5	519000
2	27/03/2015	AJAY KUMAR GARG	JAGDISH SINGH	11:14:05	11:14:05	11:14:05	31	519000
Total								**10,38,000**

From the above it was noted that –

a. The Noticee, at 10:56:54 hrs placed a sell order for 519,000 units of call option of contract "SUNP15APR1040.00CE" at a price of ₹5. This sell order of the Noticee got matched with the buy order of Mr. Jagdish Singh, who himself had placed a buy order for same quantity of 519,000 units in the same contract at same time i.e. 10:56:54 hrs.

b. Thereafter, the Noticee, at 11:14:05 hrs placed a buy order for 519,000 units of call option of contract "SUNP15APR1040.00CE" at a price of ₹31. This buy order of the Noticee got matched with the sell order of Mr. Jagdish Singh, who had placed a sell order for same quantity of 519,000 units in the same contract at same time i.e. 11:14:05 hrs.

c. Thus, the sell order placed by the Noticee at ₹5 was reversed with the same counterparty at ₹31, within 20 minutes and artificial volume generated through such non genuine trades was for 10,38,000 units of the contract.

d. The Noticee, by executing such non genuine trades, registered a negative close out difference of ₹1,34,94,000.

e. Summary of dealings of Noticee in the said contract is as follows:

Table 2 – Summary of dealings of the Noticee in contracts wherein he executed non genuine trades

S. No.	Contract Name	Avg. Buy Rate (₹	Total Buy Volume (no. of units)	Avg. Sell Rate (₹	Total Sell Volume (no. of units)	% of Non Genuine trades of Noticee in the contract to Noticee's Total trades in the Contract	% of Non Genuine trades of Noticee in the contract to Total trades in the Contract	% of Artificial Volume generated by Noticee in the contract to Noticee's Total Volume in the Contract	% of Artificial Volume generated by Noticee in the contract to Total Volume in the Contract
1	SUNP15APR1040.00CE	31.00	519000	5.00	519000	100%	100%	100%	100%

3. It was observed that:
   a) The alleged to be non-genuine trades of the Noticee were 100% of the total trades that had happened in the aforementioned contract in the market.

   b) The whole volume of 10,38,000 generated by the Noticee in the above contract due to its alleged non genuine trades was artificial volume, and further this alleged artificial volume, generated by the Noticee, also contributed 100% of the total volume in said contracts in the market.

   c) These alleged non genuine trades, executed by Noticee in above contract, had significant differential in buy rates and sell rates considering that the trades were reversed on same day.

   d) The Noticee had allegedly engaged in the non-genuine transactions in the option segment of BSE for the purpose creating false appearance of trading.

4. In view of the above, it was alleged that the Noticee, by indulging in execution of aforesaid reversal trades in Stock Options at Stock Options Segment of BSE with same entity on the same day, which were non-genuine in nature, had created false or misleading appearance of trading in the aforementioned contract traded in the Stock Option Segment of BSE. In view of the fact that these options contracts were illiquid in nature, having very small volume in trading, the Noticee allegedly created artificial volumes in Stock Options which was manipulative and deceptive in nature. Therefore, the Noticee is alleged to have violated the provisions of Regulation 3(a), (b), (c), (d), 4(1) and 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"). The text of these provisions of PFUTP Regulations are as under:

   <u>PFUTP Regulations</u>
   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 there under;
   (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 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.

5. The competent authority in SEBI *prima facie* felt satisfied that there are sufficient grounds to inquire and adjudicate the alleged violations of the provision of Regulation 3(a), (b), (c), (d), 4(1) and 4(2)(a) of the PFUTP Regulations by the Noticee and appointed Shri Suresh B. Menon, Chief General Manager as Adjudicating Officer (erstwhile AO) vide order dated May 29, 2018 to inquire and adjudge under Rule 5 of SEBI (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules, 1995 and under section 15HA of the SEBI Act, the aforesaid alleged violations by the Noticee.

6. In terms of Rule 4(1) of the Adjudication Rules read with section 15I of the SEBI Act, the notice to show cause no. SEBI/HO/EAD-1/25062/2018 dated August 27, 2018 ('the SCN') was issued by the erstwhile AO to the Noticee calling upon him to show cause as to why an inquiry should not be held against him in terms of Rule 4 of the Adjudication Rules and penalty be not imposed under Section 15HA of the SEBI Act for the aforesaid alleged violations. After seeking further time, the Noticee had filed his reply through his legal representative Mr. Bharat Raichandani, Advocate, UBR Legal Advocates, vide letter dated February 20, 2019.

7. Subsequently, by a common communication-order dated March 25, 2019, this case has been transferred to me with advise that except for the change of the Adjudicating Officer the other terms and conditions of the original orders *'shall remain unchanged and shall be in full force and effect'* and that the "*Adjudicating Officer shall proceed in accordance with the terms of reference made in the original orders".* Accordingly, after receipt of records of these proceedings an opportunity of hearing was granted to the Noticee on May 02, 2019.

8. After seeking adjournment, the Noticee availed opportunity of hearing granted to him in terms of Rule 4 (3) of the Adjudicating Rules on May 10, 2019, when Mr. Rishabh Pradeep Jain, Advocate, UBR Legal appeared before me and made submissions on the lines of the Noticee's written reply filed in this matter. The replies /submissions of the Noticee are *inter alia* as follows:

   a. The SCN proceeds on an incorrect factual as well as legal basis. The Noticee denies and counters each and every legal allegation contained in the SCN. The SCN is vague and beyond comprehension and based on surmises and conjectures. The Noticee submits that it is incumbent upon the SCN to explain in clear terms the basis as to how the transaction undertaken by the appellant attracts penalty. No evidence has been placed on record about the fact of illegal transactions, the benefit or alleged advantage flowing to the Noticee therefrom or the loss resulting to any other expression due to stock trade option by the Noticee. A mere bald allegation cannot take place of evidence.

b. The SCN proceeds on the assumption that the Noticee is the loss making entity which was deliberately making loss through their reversal trades in stock options. No entity would purposely seek to incur losses, as no prudent businessman would venture into loss. This allegation is beyond logic.

c. Reverse trades are only to avoid greater potential losses on the one side and book profits on the other side. Option contracts are one sided contract where the loss suffered, if any, by the buyer is limited only to the premium amount, whereas the loss which could be suffered by the writer of the contract (seller) is limitless. If during the period of contract the market perception of the seller (writer) changes or the market starts moving contrary to his expectations, he may, in his anxiety to cap his losses, take a reverse position. He should then put in an offer or accept an offer of a higher premium for the same option and this in effect would result in his repurchasing the contract at higher rate/ premium to avoid greater losses. This could even happen on the same day and if the options contract is illiquid, the parties in reverse trade could be the same. These are legitimate business transactions, hence, the assumption in SCN that the Noticee has indulged in transaction to create artificial units of illiquid stock options is incorrect, on facts, as well as presumption, in law.

d. There is no evidence which concludes that the transaction has manipulated BSE index. The SCN alleges that the Noticee was involved in synchronized trading (synchronized trade is one where the buyer and seller enter the quantity and price of the shares they wish to transact at substantially the same time). The Noticees has placed reliance upon the decision of the Hon'ble Securities Appellate Tribunal ("SAT") in the matter of *Ketan Parekh v. SEBI (SAT Appeal No. 2 of 2014 dated July 14, 2006),* wherein it was observed that synchronized trades *per se* are not illegal but only those which manipulate the market in any manner are the ones that are prohibited and violate the regulations. Similar view has been taken in the case of ICICI Brokerage Services Ltd.

e. The Noticee has also relied upon the observations made by SAT in *Nirmal Bang Securities Pvt. Ltd. vs. SEBI [2004] 49 SCL 421*, the then Chairman of the Board while dealing with the synchronized trades executed by the appellant therein observed as under:-

"*For the above reason, although it cannot be said that all synchronized deals are per se illegal, for the same reason, it cannot be said that all synchronized transactions are legal and permitted. All synchronized transactions which have the effect of manipulating the market are against fair market practices and hence undesirable and prohibited.*"

f. Thus, only such synchronized trades violate the Regulations which manipulates the market. Since, the impugned trades of the Noticee in the Option Segment had no impact on the market, they did not violate the Regulations. The concerned scenario in the Options contracts in this case is altogether different from that of the cash segment. In the Future and Options ("F&O") Segment there is no concept of "*change of beneficial ownership*" since what is traded in this segment are contracts and not the underlying stock or index and it is only through cash settlement that the trade is concluded and no physical delivery of any asset is involved. In this view of the matter, synchronized and reversal trades in BSE options in the F & O segment can never manipulate the market.

g. The SCN fails to prove the motive of the Noticee for making losses deliberately. The Noticee to cap his losses put in an offer or accepts an offer of a higher premium for the same option and this in effect would result in his repurchasing the contract at a higher rate/ premium to avoid losses. The Noticee had neither indulged in execution of non-genuine trade nor has created false or misleading appearance of trading in stock option segment of BSE. Further, none of the provision of the Regulation 3 and 4 of the PFUTP have been violated by the Noticee, since, he had not committed any "*fraud*" as defined under Regulation 2 of the PFUTP Regulations. Consequently, no penalty under the provisions of 15 HA of the SEBI Act can be imposed on the Noticee.

h. The Noticee submitted that, in view of the above submissions, the SCN is to be dropped.

9. I have considered the allegation levelled in the SCN, reply / submissions of the Noticee and the relevant material brought on record. The trades that are the basis of allegations in the SCN are admitted by the Noticee. The Noticee has raised technical objection that the SCN is vague and based on surmises and conjectures and no evidence has been placed on record about the fact of illegal transactions done by him. I note that the allegation that the trades carried out by the Noticee were reversal trades are directly supported with evidence from the trade log containing records of all trades and reversal trades carried out in the Stock Options segment of the BSE by him during the Investigation Period. It is to be mentioned that the SCN relies only on the trade logs which had been provided to Noticee along with the SCN. Further, it is noted that SCN *inter alia* bears clear narrative mentioning allegation in respect of Noticee for execution of alleged non genuine reversal trades resulting into generation of artificial volume in 1 Stock Option contract. Further, the alleged non genuine trades of Noticee in the said contract are described and explained by tabular representation of its contract-wise summary of dealings in said contract. Therefore, the Noticee's contentions against the validity of the SCN on these grounds are not correct and hence rejected.

10. It is to be noted that reversal trades are considered non-genuine trades if they involve an entity reversing its buy or sell positions in a contract with subsequent sell or buy positions with the same counterparty during the same day. In this regard, artificial volume is considered as the volume (no. of units) reversed in non-genuine trades, comprising both original volume and reversed volume while keeping out the volume which is not reversed.

11. Admittedly, the Noticee had indulged in 2 such reversal trades in 1 unique contracts on March 27, 2015 involving reversal of trades with same entity i.e. Mr. Jagdish Singh, in less than 20 minutes in a synchronised manner. It is noted from the trade logs relied upon in the matter that the Noticee and Mr. Jagdish Singh both had placed their respective sell-buy and buy–sell orders in exactly same time. Further, each trade involved matching of time, price and quantity of units. Thus, the volume in the

said contract on March 27, 2015 was created from the said reversal trades orders of the Noticee. Such trading pattern in illiquid Stock Options cannot occur just by accident or coincidence. Such synchronization as found in this case in an illiquid market with anonymous trading indicates a prior meeting of minds and arrangement with a view to execute the reversal trades at a pre-determined price for non-genuine purposes.

12. As held by Hon'ble ("SAT") in the matter of *Ketan Parekh and Nirmal Bang* case as relied by the Noticee the synchronised trades *per se* are not illegal but those which manipulate the market in any manner are the ones that are prohibited and violate the regulations. Further, manipulative device and artifice can be inferred from the facts and circumstances of a particular case as held by Hon'ble SAT in *Ketan Parekh* case that - *"The nature of transactions executed, the frequency with which such transactions are undertaken, the value of the transactions, 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."*

13. Further, Hon'ble Supreme Court in the matter of *SEBI v Rakhi Trading Private Limited (Civil Appeal Nos. 1969, 3174-3177 and 3180 of 2011 decided on February 8, 2018)*, observed 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 naive 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…..*" In the same matter, Hon'ble Supreme Court further held 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 had only misleading appearance of trading in the securities market*". With regard to such reversal transactions, Hon'ble Supreme Court also held in the *Rakhi Trading case* 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*".

14. Therefore, the contention of the Noticee that synchronized and reversal trades in BSE options in the F & O segment cannot manipulate the market is not correct. The synchronized trading with same counterparty at same time for same quantity at same price and reversal of transaction with wide variation in price of the reversed trades in the same contract in a short time without any basis, all indicate that the trades executed by the Noticee were not genuine trades and being non-genuine, created an appearance of artificial trading volumes in the contract in question.

15. The impugned reversal trades were carried out by the Noticee in an illiquid Stock Options contracts where there was no participation of public. Reversal trades were undertaken by the Noticee with his counterparty with a predetermined arrangement to book profit or losses respectively, and, therefore, the parties to the trades were not trading in the normal sense and ordinary course of business. Investigation has shown amount of profit / loss of the counterparties to the trades as a result of

such non-genuine trades. 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 counterparties in totality. When the impact of artificial volumes created by the two counterparties is seen as a whole, the making loss or profit is immaterial as the charge in this case is of creating false or misleading appearance of trading in the aforementioned contract.

16. These non-genuine and deceptive trades are covered under the definition of '*fraud*' and dealing of Noticee were '*fraudulent*' as defined under Regulation 2(1) (c) of PFUTP Regulations. Further, it cannot be ignored that synchronization of trades in pre-determined manner had an adverse impact on the fairness, integrity and transparency in the securities market.

17. In view of the above, I find that the allegation of violation of regulations 3(a), (b), (c), (d), 4(1) and 4(2)(a) of PFUTP Regulations by the Noticee stands established. Thus, I hold that the Noticee liable for penalty under Section 15HA of the SEBI Act which reads as under:-

"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."

18. While determining the quantum of penalty, it is important to consider the factors stipulated in Section 15J of the SEBI Act which reads as follows:-

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."

Explanation.—*For the removal of doubts, it is clarified that the power of an adjudicating officer to adjudge the quantum of penalty under sections 15A to 15E, clauses (b) and (c) of section 15F, 15G, 15H and 15HA shall be and shall always be deemed to have been exercised under the provisions of this section;*

19. It is not possible to determine the consequent loss caused to investors as a result of the default as found in this case. It is worth considering that generally, there is NIL or negligible participation of the public in the trading in such illiquid Stock Option contracts. When the impact of artificial volume created by the two counterparties is seen as a whole, it is not possible from the material on record to quantify the amount of disproportionate gain or unfair advantage resulting from the artificial trades between the counter parties or the consequent loss caused to investors as a result of the default. However, considering the fact that the trades of the Noticee in one Stock Option contract

which resulted into 100% artificial volume generated out of the non- genuine trades of the Noticee, I am of the view that such fraudulent trades deserve imposition of monetary penalty of the Noticee under section 15HA of the SEBI Act.

20. Considering all the facts and circumstances of the case including the aforesaid mitigating factors and exercising the powers conferred upon me under section 15I of the SEBI Act read with Rule 5 of the Adjudication Rules, I hereby impose, a monetary penalty of ₹ 5,00,000/- (Rupees Five Lakh Only) on the Noticee *viz.* Mr. Ajay Kumar Garg under section 15HA of the SEBI Act. In my view, the said penalty is commensurate with the violations committed by him in this case.

21. The Noticees 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 through e-payment facility into Bank Account the details of which are given below:

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

22. The said demand draft or forwarding details and confirmation of e-payment made in the format as given in table below should be sent to "*The Division Chief, EFD-DRA-I, Securities and Exchange Board of India, SEBI Bhavan, Plot no. C- 4 A, "G" Block, Bandra Kurla Complex, Bandra (E), Mumbai - 400 051*" and also to e-mail id:- tad@sebi.gov.in

1	Case Name	
2	Name of the 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)	

23. In the event of failure to pay the said amount of penalty within 45 days of the receipt of this Order, recovery proceedings may be initiated under section 28A of the SEBI Act, 1992 for realization of the said amount of penalty along with interest thereon, *inter alia*, by attachment and sale of movable and immovable properties.

24. In terms of Rule 6 of the Adjudication Rules, copies of this order are sent to the Noticee and also to SEBI.

Date: June 04, 2019 **Santosh Shukla**
Place: Mumbai **Adjudicating Officer**