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Synchronized Trading as Manipulative Device: A Critical Legal Analysis

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ABSTRACT

Synchronized trading results in a deception of the market, and is extremely difficult to detect. The basic objective of this paper is to cull out the origin of screen-based trading and the principle of anonymity, as the pillars of the Indian securities markets. This paper also discusses the types of deceptive devices employed by parties to evade regulators in India. It also focuses on fairly determining the various grounds for the determination of synchronized trading in India. The factors in respect of synchronized trading have not been mentioned/ ascertained in India, which make its detection difficult. It is to be noted in this context that synchronized trading though has been used as a term by the SEBI freely, it lacks a particular description/ definition in the Indian context. In this light, the paper shall attempt at indicating those factors which may lead to a better identification and resolution of practices, termed as synchronized trading.

Keywords: Synchronized trading, Securities and Exchange Board of India (SEBI).

I. INTRODUCTION

The origin of the stock market can be traced to ancient Rome in the second century BC.² The Dutch East India Company issued the first paper shares in 1602. This concept was so successful that it quickly spread to other maritime nations of the day, including Portugal, Spain, and France.

As the volume of shares expanded, it necessitated the establishment of an organized marketplace for their exchange. As a result, stock traders convened at a London coffeehouse that served as a marketplace. They gradually gained control of the coffeehouse, renaming it the "stock exchange" in 1773. Thus, was founded the world's first stock exchange, the London Stock Exchange. The concept spread to the American colonies as a result of a 1790 transaction in Philadelphia.³

The stock exchange has certainly undergone a multitude of changes since its origin. Waves of

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² B. Mark Smith, *A History Of The Global Stock Market: From Ancient Rome To Silicon Valley* (1st edn, University Of Chicago Press 2004).

³ Laura Bramble, 'How the Stock Market was Started by Whom', CHRON < <https://smallbusiness.chron.com/stock-market-started-whom-14745.html>.> accessed 6 July 2021

new developments often sweep away the old and usher in the new, as did the introduction of electronic stock exchanges almost 50 years ago.⁴

Trading in Securities must be transparent to make a healthy market. To ensure integrity of market various steps are taken by authorities which will be discussed in the paper. Synchronized trading is not define under law and to prove that it is a kind of deceptive devices used by players in the market, different authorities will be referred. In this reference Supreme Court of India in case of Securities and Exchange Board of India v. Rakhi Trading Private Limited (Supreme Court, 2018) said:

“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.”

In the lack of substantive literature discussing this type of manipulative trading exclusively, the author has constantly referred to court’s and tribunals’ interpretations of the term in order to examine the issue of synchronized trading.

Bernard Baruch, who made almost all of his fortunes through the stock market once stated that “The main purpose of the stock market is to make fools of as many men as possible”.⁵ It may be said that in today’s day and age, it is the brokers who make fools of men, and not the stock market itself. However, with the evolution of the stock market, its users have evolved too. They are not as clueless as before. A robust stock exchange of today must seek to establish a level playing field for all investors, and be able to handle all the scrutiny levelled at it.

Screen-based trading

The screen-based trading has been the newest development in this field and this is what the project shall deal with. From an Indian perspective this is strictly defined as a form of trading It combines information transmission and financial market trading through the use of contemporary telecommunications and computer technology.⁶

⁴ Fischer Black, ‘Towards a Fully Automated Exchange’(1971) Financial Analyst Journal, 27, 4. <<https://www.tandfonline.com/doi/abs/10.2469/faj.v27.n4.28>> accessed 8 July 2021

⁵ Bernard Baruch Quotes, <https://www.brainyquote.com/quotes/bernard_baruch_181388>. accessed 6 July 2021

⁶ Screen-based trading, NiSM Certification <<http://www.nism.ac.in/certification/index.php/component/seoglossary/1-glossary/screen-based-trading>>_accessed 20 June 2021

Prior to the establishment of the National Stock Exchange, trading on India's stock exchanges was conducted by open outcry, without the use of information technology for instant matching or recording of trades.⁷ This floor-based trading had its inherent vices –

1. It was time consuming and inefficient.
2. Physical trading - put restrictions on trade volumes and the rate at which new information was reflected into prices.
3. The new and dynamic India was growing at a faster pace than floor-based trading could handle.
4. Open outcry system was an open door to market manipulation.
5. Physical delivery of shares, a bulky settlement procedure were obvious flaws.

In response to this arbitrary, inadequate, non-transparent, hardly regulated system, a masterstroke was envisioned. The NSE was the first to introduce the screen-based trading system (SBTS) in 1992. SEBI permitted all exchanges to effect screen-based trading across India.

In this system, a member enters the quantity of shares and the price at which he wishes to trade into the computer. The transaction is initiated as soon as a trading member's quote punches a matching sale or purchase quote from the counterparty. SBTS electronically connects buyer and seller in an order-driven system or discovers the best price for the client in a quote-driven system, thereby saving time, money, and risk of error, as well as reducing the likelihood of fraud.

The benefits of screen-based testing are several —

1. It enables remote players to transact with one another. This contributes to the markets' increased liquidity.
2. Because trades are completed at a high rate of speed and a large number of players can trade concurrently, price-sensitive information is incorporated into prevailing prices more quickly.
3. As a result, this improves the market's informational efficiency. It enables market participants to observe the entire market, which contributes to enhanced market transparency

⁷ Ashley Coutinho, *Electronic trading: The NSE trump card that changed stock market dynamics*, BUSINESS STANDARD, November 8, 2019 < https://www.business-standard.com/article/markets/electronic-trading-the-nse-trump-card-that-changed-stock-market-dynamics-119110701804_1.html>. accessed 25 June 2021

and investor trust.

4. The NSE implemented a nationwide screen-based trading system, resulting in an entirely transparent trading mechanism.

5. Its accessibility to trading and availability of information make it an exceptionally investor-friendly platform.

The anonymity it offers with respect to trades makes it market oriented. Therefore, it is the best of both worlds.

II. PRINCIPLE OF ANONYMITY

Anonymity as a condition sine qua non to trading between parties is an established principle.

There are no market makers, and the entire process is order-driven, meaning that investors' market orders are automatically matched to the best limit orders. As a result, both buyers and sellers maintain their anonymity.

This is further illustrated with the help of two landmark judgements:

1. Ajmera Associates Pvt. Ltd. v. SEBI⁸

It is undisputed that the trading method used on stock exchanges is a blind trading system that ensures the traders' complete anonymity. While executing an order (buy or sell), the broker has no way of knowing who the counter party is or even the counter party broker at the moment the transaction is placed through the system.

In other words, the trading system forbids buyers and sellers from interacting with one another except via the trading system. When a buy order is matched with a sell order, a transaction is conducted, and the system does this matching on a price time priority basis.

2. VG Capital Market Private Limited v. SEBI⁹

The trading system on the exchanges is based on the principle of anonymity. The buyer does not know who the seller is and seller cannot know who the buyer is. In other words, the buyer should buy the shares without being concerned as to who the seller is and similarly the seller should sell the shares in the market without being concerned about the buyer and it is the system which determines the buyer and the seller by matching the buy and sell orders.

On a screen-based trading, the best buy order will match the best sell order subject to price time priority. It is true that before any buy and sell order can result in a trade they must match but

⁸ SAT, 2010.

⁹ SAT, 2009.

this matching must take place through the system without the intervention of any human element.

This Paper shall look at the shake-up in the screen-based trading through introduction of the deceptive devices. Part I has described the movement from traditional basis of trading to a screen based trading. Part II shall deal with the various regulations and provisions which prevent deceptive trades on the market. Furthermore, Part III shall discuss the various deceptive devices in order to provide a background to Part IV which shall actually cover synchronized trading, the crux of the Paper. Finally, Part V shall deal with the conclusion and mention the requirement for evolution in this sphere in order to be able to regulate it better.

III. CONTOURS OF MARKET MANIPULATION AND SEBI

The Securities and Exchange Board of India ('SEBI') was founded in 1988 as a non-statutory body charged with the responsibility of regulating the securities market. It became an autonomous organization on 12 April 1992, when the Indian Parliament passed the SEBI Act 1992. It was promoted to the position of securities market watchdog as a result of this Act.

Market manipulation is a form of market abuse in which an intentional attempt is made to obstruct the free and fair operation of the market and to generate artificial, false, or misleading appearances regarding the price or market for a product, security, commodity, or currency.¹⁰

These kinds of market manipulations, frauds, insider trading etc. are what lead to the biggest scams in stock market history, for example the Harshad Mehta scam, Ketan Parekh scam and the infamous Satyam scam.¹¹

SEBI has come up with various publications with an aim to regulate the securities market, some of which will be illustrated below -

SEBI Act of 1992

- Inserted Section 12A in the Act through the Amendment Act of 2002.
- This section prevents any person from manipulating the market, either directly or indirectly.

Bulk deal circular dated September 14, 1999

- This circular provides guidance in respect of negotiated deals.

¹⁰ Tom Lin, *The New Market Manipulation*, 66 Emory L. J. 1259 (2017). <<https://scholarlycommons.law.emory.edu/elj/vol66/iss6/1>> accessed 20 June 2021

¹¹ Rajarshi Bose, *3 Biggest Scams in Indian Stock Market*, TRADE BRAINS, February 24, 2020 <<https://tradebrains.in/biggest-scams-that-shook-indian-stock-market/>> accessed 10 July 2021

- All such deals to be executed like any other normal trade.

Bulk deals circular dated January 14, 2004

- This circular provides guidance in respect of bulk deals.
- It provides that execution of trades which are in respect of 0.5% of the total equity shares of the listed company shall be disclosed.

Block deal circular dated October 26, 2017

- A previous circular in 2005 prescribed guidelines for execution of large trades through a separate trading window.
- This circular review the 2005 circular and announces the establishment of two block deal windows.

The Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market), Regulations, 2003 ('PFUTP Regulations')

This regulation is the primary instrument aimed at tackling market manipulation, and through its wide and all-encompassing language, it includes all forms of manipulative devices. The scope of this paper being limited to manipulative trading devices, with special reference to synchronized trading, only the relevant provisions have been included.

Regulation 3

No person shall directly or indirectly:

- (a) Deal in a fraudulent manner.
- (b) Use or employ any manipulative or deceptive device in contravention of the Act or Rules or Regulations.
- (c) employ any device, scheme or artifice to defraud in connection with dealing.
- (d) engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person.

Regulation 4

Prohibition of manipulative, fraudulent and unfair trade practices

1. No person shall engage in fraudulent or unfair trade practice.
2. Dealing in securities to be fraudulent or unfair, if it involves:
 - a. indulging in an act which creates false or misleading appearance of trading.

- b. dealing in a security with no intent to transfer beneficial ownership.
- e. any act or omission amounting to manipulation of the price of a security.

Recently, SEBI has considered using Artificial Intelligence (AI) and blockchain technology to fight market manipulation via social media.

- Social media platforms have emerged as critical tools for market manipulation, and SEBI may substantially benefit from the application of emerging technology such as natural language processing (NLP) and big data analytics in this area.
- Blockchain technology has the potential to be utilised for clearing, settlement, and record-keeping, as it enables the maintenance of records in distributed ledgers while also serving as a single source of truth.¹²

In this light, it can be viewed that India has a web of laws which may be implemented in order to disallow such deceptive transactions as are being effected on the stock exchanges. However, the problem lies at the end of interpretation of these laws as will be seen in the parts to follow. It will be seen how the subjective attitude of the members of the SEBI and SAT renders these laws to be merely determined based on their understanding of the market. Importantly, the requirement of intention though not strictly imputed by the law, has been advanced by these members in order to decide culpability. It will be seen that this intention though it may enable to catch certain people red-handed, really gets in the way of certain transactions where the threshold is not met. The authors shall look at these concepts in the following parts, especially in the part which exclusively deals with synchronized trading.

IV. TYPES OF DECEPTIVE DEVICES

One of SEBI's primary objectives is to regulate and protect the interests of investors in the securities market, which is critical to the market's functioning.

For instance, from 25th April 2008 to 13th April 2011, Sahara issued Optionally Fully Convertible Debentures (OFCDs) to investors without SEBI approval and collected about Rs.17,400 crore. SEBI, recognizing the danger to investors' interests, took up this matter and ordered Sahara to repay the full amount received to investors with a 15% interest rate.¹³

Thus, SEBI strives to protect the investors from becoming fodder for the selfish interest of higher-ups. To that effect, SEBI seeks to counter any deceptive devices used by parties.

¹² *SEBI to use AI, blockchain tech to fight market manipulation via social media*, BUSINESS LINE, January 23, 2020 <<https://www.thehindubusinessline.com/markets/social-media-key-tool-for-market-manipulation-ajay-tyagi/article30633275.ece>> accessed 20 July 2021

¹³ Securities and Exchange Board of India (SEBI) v. Sahara India Real Estate Corporation Ltd. (2013) 2 SCC 733.

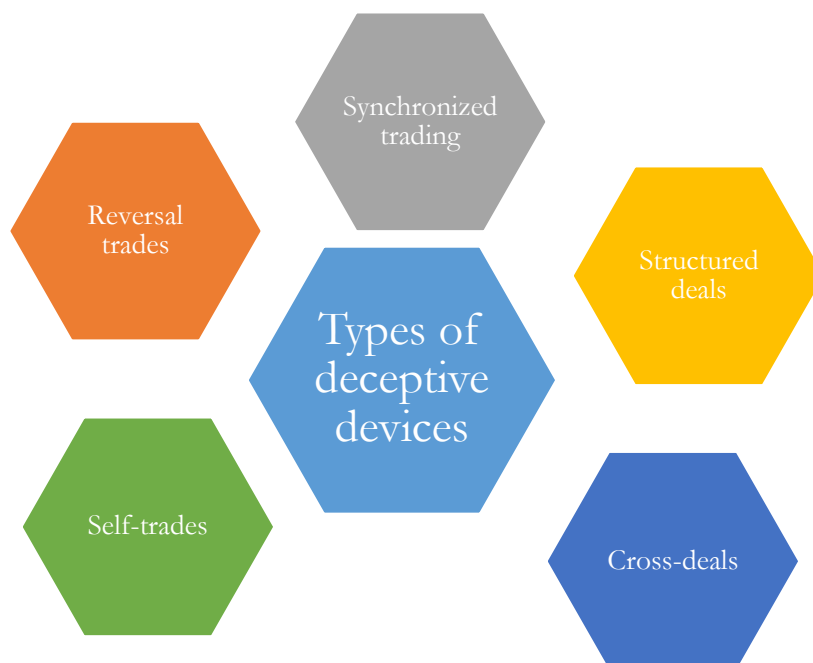
Deceptive devices refer to mechanisms adopted by parties which may violate the provisions of the PFUTP Regulations.

The PFUTP Regulations were enacted to protect investors' interests and to prohibit unfair and fraudulent trade practices that might jeopardize the securities market's integrity. In *SEBI v Kanaiyalal Baldevbhai Patel and Ors.*,¹⁴ The Court noted that the Regulation's object and purpose are to protect the investing public and honest businessmen.

Its objectives are as follows:

- to prevent the public from being exploited by fraudulent schemes and worthless securities through misrepresentation;
- to present the investor with accurate and complete information
- to safeguard honest businesses seeking funding through precise disclosure,
- to guard against exploitation in the face of competition from deceptive securities marketed to the public, and
- to re-establish the prospective investor's faith in his capacity to select sound assets.

This section of the project shall focus at some of the deceptive devices that fall under the purview of these regulations.



¹⁴ [2017] 141 CLA 254 (SC).

Fig 1- Types of Deceptive Devices

(A) Reversal trades

It means reversing the buy and sell positions with subsequent sell or buy trades on the same day with the same counter party.

In addition to not being executed in the normal course of trading, they are alleged to be non-genuine trades because they do not follow basic trading principles and allegedly lead to a false or misleading appearance of trading through the generation of artificial volume, and as a result were deceptive and manipulative, according to the complaint. Artificial volume is defined as the volume (number of units) reversed in both legs of a reversal trade while excluding the volume (number of units) that is not reversed in any leg of the trade.

Why its deceptive: This means a change in liquidity of the stocks, as well as incurring the possibility of driving the price up or down.

(B) Synchronized trades

These trades are completed by simultaneously placing a purchase and sell order for the exact same quantity and rate within a one-minute period. The word "synchronised trading" does not have a statutory definition. In the absence of a statutory definition, the term has been defined by courts through case law.

Why its deceptive: They result in creation of artificial volume and manipulation of the last trading price. They also influence the price.

(C) Self-trades

Self-trades are transactions in which the buyer and seller are one and the same. These exchanges do not reflect a change in the security's beneficial ownership.

Previously, the stance on self-trades was that they generate counterfeit or artificial volume in the market and provide a false and deceptive appearance of trading in the scrip at the exchange; thus, they are per se illegal, improper, and in violation of securities regulations.

SEBI issued a new policy on May 16, 2017 stating that purpose is required to demonstrate manipulation in the instance of self-trades and that inadvertent or unintentional self-trades are not covered by the PFUTP Regulations. As a result, SEBI does not penalise such deals but rather looks at the client's/intent broker's.

Why its deceptive: There is no change in beneficial ownership, and such trading increases the liquidity in the scrips trade. These types of trades actually give a false appearance of trading,

whereas actually there is no trade happening.

(D) Structured deals

These deals encompass a series of transactions between the same parties through which individuals or entities may trade in securities. This mechanism is adopted in order to avoid any regulatory inspection through dividing of one transaction into various transactions.

Why its deceptive: These deals may be considered to form a component of synchronized trading and are deceptive due to all those reasons in connection to synchronized trading, as stated by SEBI in the Bhanwar Singh Paliwal order.¹⁵

(E) Cross deals

A cross deal involves the use of a uniform broker by both the parties in order to execute the buy and sell orders. This makes it very convenient for the broker to match their trades. Cross deals are generally not illegal and may be considered as such only when they tend to manipulate the market. In this light the following are the deceptions which can be affected by cross deals.

Why its deceptive: If misused, it may cause increase in volatility of shares, acceleration of price, no change in beneficial ownership, depressing of price.

Considering there are so many deceptive devices to trade, the focus of this Paper should be on synchronized trading in order to ascertain its factors and those conditions which influence it more. It has to be noted that there is some amount of certainty under the other deceptive devices as have been mentioned, however, a discussion of synchronized trading will also lead to the discussion of the other deceptive devices. The selection of synchronized trading has been made keeping in mind that it is the most difficult to determine and punish.

V. DETERMINATION OF SYNCHRONIZED TRADING

This Paper shall only focus on the specific determination of incidents which may be stated to be synchronized trading as has been mentioned before. This enquiry is incomplete without looking at the factors which may be considered for the determination of synchronized trading in India. In order to arrive at the transactions which may be called synchronized trading, the author claim that the process is very rigorous and involves due attention of the various statements of the SEBI and the SAT. As an opening sentence, the author note that the SEBI and SAT have very loosely used the term “synchronized trading” in order to classify certain transactions. We shall consider the factors one after the other, and determine how there can be

¹⁵ SAT, 2013.

better definition of the term in the Indian context.

1. Change in Price of the Scrips

The first factor concerns the change in prices of scrips. This is a usual factor which may be attributed to depress or increase the prices. If there is a sudden change in the prices of the scrips, induced with the intention to gain out of the market results in synchronized trading. There are certain landmark cases under this head which the authors have compiled which deals with the case of changes in price.

a) **SEBI v. Shankar Lal Chokhany**¹⁶

The price of Ranbaxy Laboratories Limited rose pursuant to which the Appellant investigated in the trading of Ranbaxy's scrips. During the investigation period between January 1999 and October 1999, the following details in respect of the scrips were noted:

i) **Volume of the scrips traded:**

A total of **74 synchronized trades** were carried out by the Respondent while trading in Ranbaxy's scrips.

ii) **Price of the scrips traded:**

The price of the scrips rose from **Rupees 270 to Rupees 1200** during the investigation period.

The charge of synchronized trading was upheld by the Appellant and the registration of the Respondent was suspended for a period of 6 months through the impugned order. The judgment in the matter was given by one Mr. VK Chopra, who noted that he was of the view that several synchronizations of trades could not be treated as mere coincidence. In such cases, he stated that the prices and quantities had been negotiated outside the system and orders had been executed simultaneously. He observed that all the 74 transactions which had been entered into by the party gave an impression that they were all synchronized and traded to create artificial market, otherwise there was no possibility of such perfect matching of quantity price, etc. In view of these factors, he found that the broker had put these trades with a view to create misleading appearance of trading. This synchronization was noted to tamper with price discovery mechanism of stock exchange and also militate against the concept of transparency. The broker had entered into several synchronized deals. These trades abetted in creating artificial volumes and false market in the scrip of Ranbaxy Laboratories Ltd. Accordingly, it is to be noted that such rises in the price as from Rupees 270 to 1200 was seen to be artificially inflated in order for the company to make profit. Such artificial inflation outside the system

¹⁶ SEBI (2007).

with a view to dupe the general traders was seen to be synchronized trading.

b) SEBI v. Delhi Securities Limited¹⁷

The shares of Shonkh Technologies International Limited (“STIL”) were listed at the Delhi as well as the Bombay Stock Exchange. It was noted that there was a constant rise in the price of these shares for a month. This spurred the SEBI to investigate the matter and it was found out through this investigation that certain entities had deliberately attempted at creating liquidity and volumes in the shares of STIL at the DSE. This order of the SEBI dealt with this issue and another connected issue pertaining to synchronized trading. During the investigation period, the following details were noted:

i) Volume of the scrips traded:

Brokers were found to have participated in systematic purchases and sales of STIL shares. One of the brokers was detected buying 9000 shares and selling 16100 shares, which represented 26.5 percent and 47.42 percent of the overall buy and sell volume at the DSE, respectively.

ii) Price of the scrips traded:

The price of the scrips rose from Rupees 300 on its listing to Rupees 460 within a span of one month. Subsequently, it decreased to Rupees 330, two months after the shares had been listed.

The SAT order also mentioned that there were certain factors in addition to the fluctuations in the prices of the shares. These related to the creation of liquidity and volumes in the newly listed shares of STIL, connection between the clients which worked together in order to enter into synchronized trade and trading at prices higher than the last traded price continuously. The Tribunal noted that the price of the shares of STIL which were allowed to trade at DSE on August 16, 2000 at Rs. 300/- increased to Rs. 460/- on September 28, 2000. The Broker had traded in the shares of STIL on all trading days between August 16, 2000 and August 23, 2000 and his trades accounted for 99%, 52%, 100%, 100%, 100% and 96% of the total buy and sell volume at DSE in the shares of STIL. It can be seen that the trades in the shares of STIL at DSE were low and that the trades of the Broker accounted for either the entire or the majority of such volume. The Tribunal considered the facts and circumstances of the case, wherein the trades in an *illiquid scrip* were executed between common set of brokers and clients regularly at a higher price as mentioned in this order, where the Broker was aware of the counterparty. The prices of synchronized trades executed by the broker were higher by 2.08% as compared to the previous day's closure price. The Tribunal noted that the broker had only entered into the trades with an

¹⁷ SAT (2007).

intention to attract other persons to deal in the shares by giving them a misleading appearance of trading in the shares of STIL.

c) **M/s. Bubna Stock Broking Services Limited v. SEBI**¹⁸

This case dealt with two appeals which had identical questions of law and fact. The Respondent carried out investigation in the trading of scrips of Rohan Finance and Securities Limited whose shares had seen a sharp rise in the Calcutta Stock Exchange. The Appellant, a registered stock broker was seen involved in the group of brokers and clients who had raked up the prices of the scrips of Rohan Finance and Securities Limited. The investigation took place between 24 January and 29 July, 2004 and it was noted that the prices of shares rose during the investigation period between Rupees 9.25 to 321. The Tribunal noted that in the present case also the buy and sell orders were put into the system at almost the same time for the same quantity and at the same rate. The Tribunal claimed that it was obvious that the object of the appellant and its clients was to defeat/ manipulate the price and order matching mechanism of the Stock Exchange. It was noted that the appellant had intentionally manipulated the system mechanism in order to execute synchronized trades.

Conclusion: It can be noted that the change in price either positively or negatively can be considered after the execution of trade, but it is not an independent factor. This includes factors like reverse trades, related parties and cross-deals. Therefore, the determination of synchronized trading in respect of cases where there is a price rise can only occur when these other factors, being complementary in nature co-exist.

2. Volume of Scrips Traded by a Party

The second factor concerns the volume of the scrips traded by the parties. This is a usual factor which may be attributed to increase in the amount of trading for those shares. If there is a sudden spurt or depression in the trading volume of the scrips, it may very well point towards a case of synchronized trading. There are certain landmark cases under this head which the authors have compiled which deals with the volume of trading in certain scrips.

a) **Networth Stock Broking Limited v. Securities and Exchange Board of India**¹⁹

Between 1 August and 16 October 2002, the Appellant, a licensed stock broker, performed trades on behalf of its clients in the scrips of GG Automotive Gears Limited. The impugned order found the Appellant guilty of engaging in synchronized trades by artificially inflating the volume of the company's scrip, which resulted in an increase in the scrips' price. Throughout

¹⁸ SAT (2009).

¹⁹ SAT (2012).

the course of the examination, the following details were noted:

- i) Volume of scrips traded: During the investigation period, 4,28,749 shares were traded in a circular fashion, accounting for 19 percent of the total volume of shares moved.
- ii) The price of the scrips traded: During the investigative period, the shares traded at a price of Rupees 23.30.

The Tribunal found that all four brokers, including the appellant, followed a common pattern of circular trading, indicating synchronization in order placement, resulting in false volume in the company's stock, which resulted in an increase in the scrip's price. Following that, the Tribunal noted that the appellant operated as a broker for one of the parties, implying that he was a party to the client's game plan for executing matching deals. The Tribunal decided that the broker may reasonably deduce that the continuous trades performed in a circular pattern between the same parties were executed with the intent to deceive the market and manipulate the trading of other traders. The huge volume of trades, which accounted for 19 percent of all deals conducted during the investigation period, was the key cause for the case to be held in synchronized trading.

b) M/s. Triveni Management Consultancy Services Limited v. Adjudicating Officer, Securities and Exchange Board of India²⁰

Appellant was a broker who facilitated trading in the scrips of Asian Star Company Limited (“ASCL”). The Respondent began investigation of ASCL’s scrips following the rise in its price and observed that the Appellant had the highest concentration of circular trade in ASCL’s securities. Subsequent to the investigation, the Respondent noted that the Appellant was advising clients belonging to the “Mehta group” in order to drive the price of ASCL’s scrips. The Appellant was thereby held liable through the impugned order being appealed, on the ground of engaging brokers in execution of synchronized and structured deals as part of circular/reversal trades with other Mehta Group Entities. In light of the same, the Respondent imposed a total penalty of Rupees 25 lakhs through the impugned order.

In the BSE, the following particulars were noted by the Respondent between October 10, 2008 and November 20, 2008:

- i) **Volume of the scrips traded:** 1974219 shares which were traded in such a form that 87.83% of the total market volume and 72.33% of the total number of trades in the scrips had been synchronized. Out of this, the Appellant was involved in the purchase and sale

²⁰ SEBI (2013).

of 26.25% of scrips.

- ii) **Price of the scrips traded:** The price rose by 18.57% in the period- from Rupees 1240 to 1306.15 when the SENSEX fell by 19.73%.

The Board noted that it was abundantly clear that the Appellant was deeply involved in manipulating volume and thus the price of the ASCL scrip by creating artificial volumes in the scrip, placing orders in his clients' accounts without their authorization, and finding counter parties for his clients' buy and sell orders from within the Mehta Group through the use of reversal trades. Additionally, the Tribunal noticed that the Appellant engaged in synchronized trading of 26.25 percent of the total market trade in ASCL's scrips. By demonstrating the Appellant's high volume of trading, it was established beyond a reasonable doubt that he was engaged in synchronized trading and manipulation of ASCL scrip for the purpose of increasing volume and thus price, by creating the false impression of frequent trading of an otherwise illiquid scrip, and by convincing investors to invest in ASCL scrip through the creation of artificial volumes.

Conclusion: Increase in trading volume can be considered after the execution of trade and may reasonably serve as an independent factor in cases of determination. Different from the fluctuations in the price, this factor can be used independently where the trading in the scrips creates further avalanche in the stock market, by changing price and increasing trading in the scrips.

3. Varying the Last Trading Price

The last trading price for a scrip is the price of closing for a stock for that day. There are certain brokers who intend to make the best out such a price by pushing it up on a subsequent trading day to indicate that there has been a positive movement in the stocks. Such movement can be very easily executed with the help of synchronized trading and may help in creation of artificial volumes and more trading in respect of those scrips. This part shall discuss cases in that regard to show the cases in which such varying of last prices may be referred to as a synchronized trade.

a) **Usha Mehta v. SEBI**²¹

Appellant was a client who traded in the scrips of Asian Star Company Limited ("ASCL") through various brokers. The Respondent began investigation of ASCL's scrips following the rise in its price. Subsequent to the investigation, the Respondent noted that the Appellant

²¹ SAT (2013).

artificially influenced the price of ASCL's scrips, being a part of the "Mehta Group." Thus, the Appellant was held accountable for engaging brokers to execute synchronized and structured agreements as part of circular/reversal trades with other Mehta Group Entities, as set forth in the impugned order under appeal.

Between October 10, 2008 and November 20, 2008, the Respondent made the following observations regarding the BSE:

- i) Volume of scrips exchanged: 1974219 shares traded in a manner that synchronized 87.83 % of total market volume and 72.33 % of all scrips trading.
- ii) The price of the scrips traded increased by 18.57 % over the time, from Rupees 1240 to 1306.15, whereas the SENSEX declined by 19.73%.

The Tribunal stated in this matter that the Appellant had connections to counter-party clients and Mehta Group entities, and performed a large number of synchronized trades with them, placing orders higher than the last trading price and manipulating the price of the company's scrip. The Tribunal noted that the fundamental rationale for convicting the Appellant was that its trading in the scrips accounted for a sizable portion of the entire market activity, both in terms of volume traded and number of trades conducted. This was accomplished by constantly placing orders above the previous trading price in order to align with the counter-party and ensure that the prices for the scrips continued to rise.

b) JHP Securities Private Limited v. Securities and Exchange Board of India²²

The Tribunal stated in this matter that the Appellant had connections to counter-party clients and Mehta Group entities, and performed a large number of synchronized trades with them, placing orders higher than the last trading price and manipulating the price of the company's scrip. The Tribunal noted that the fundamental rationale for convicting the Appellant was that its trading in the scrips accounted for a sizable portion of the entire market activity, both in terms of volume traded and number of trades conducted. This was accomplished by constantly placing orders above the previous trading price in order to align with the counter-party and ensure that the prices for the scrips continued to rise.

During the investigation period, the following details were noted:

- (i) **Volume of the scrips traded:** The Appellant had purchased 28.5% of the total market volume of shares while trading in the scrips of GIL and sold 26.78% of the total market volume while trading in the same scrips.

²² SAT (2014).

- (ii) **Price of the scrips traded:** The price during the period rose from Rupees 2.94 to Rupees 51.81 through the trading by the Appellant.

The Tribunal found that the 25% of trades in the scrip, both on the buy and sell side, occurred during IP over nearly two years for its six connected entity clients. This was done with the goal of manipulating the market by placing orders above the LTP in GIL's scrip at a time when the business's promoters were having difficulty exiting due to the acquisition of a sick company that the promoters were unable to resuscitate. Despite having held the promoters' shares for an extended period of time, the NG Group purchased the majority of the promoters' shares at a manipulative premium, and this was not a regular market transaction. Such price rises further induced gullible investors to jump in and invest in the ill-liquid scrips of GIL only in order to give a decent exit to its promoters.

Conclusion: The deliberate effort to revise the last trading price through orders is a factor to be considered for the determination of synchronized trading, but it is not independent in nature. Usually, it requires the presence of other factors like matching of trades and related parties who execute trades at higher prices with an intent to raise the prices of the stocks, as was clearly observed in the JHP Securities case above.

4. Intention of the Participant

The intention of the participant seems to play a major role in determination of whether a certain trade may be referred to as a synchronized trade. There are instances where the SEBI and SAT have made this clear. It undoubtedly plays a major role in the decision of whether a trade may be attributed as a manipulative and deceiving device, so as to constitute a synchronized trade.

a) **Ketan Parekh v. SEBI**²³

This order of the Securities Appellate Tribunal sought to dispose a bunch of 9 appeals based on common questions of law and fact in relation to Ketan Parekh and entities connected to him.

A show cause notice was served upon the Appellant for the alleged price manipulation in the scrip of Lupin Laboratories. The Appellant denied all the allegations and stated that the movement of price of such a large company was dependent on numerous facts. The Respondent while examining the allegations however, noted that:

- (i) The scrips of Lupin made a movement different from scrips of other pharmaceutical companies.
- (ii) On various instances, the brokers through whom the scrips were traded, placed orders

²³ SAT (2006).

for them at a higher price than the prevailing market price.

As a result of these findings the Board concluded that the price rise in the scrip of Lupin was artificial and that Ketan Parekh and his entities were primarily responsible for creating a higher price for the scrip. The Appellants were therefore held guilty of creating false or misleading appearance of trading in the securities market. This is the impugned order being appealed against. In deciding whether the entire trading could be regarded as fictitious and synchronized trade, with an intent to deceive the trading populace, the Tribunal noted that in normal instances a case of synchronized transaction between genuine parties would not be illegal or violate the terms of the regulations. However, a trade executed with an intent to “manipulate the market or if it results in circular trading or is dubious in nature and is executed with a view to avoid regulatory detection or does not involve change of beneficial ownership or is executed to create false volumes resulting in upsetting the market equilibrium” would be fictitious in nature and pulled out as being synchronized. Accordingly, it is clear from this decision that the Tribunal pays immense importance to the existence of intent in respect of the trades in India. In this case, the Tribunal held that the Appellant did not intend to hike the prices of Lupin, and was held guilty only of raising short term finance from the market by artificial sale and purchase of the shares.

b) Magnum Equity Broking Limited v. SEBI²⁴

The Appellant is a stock broker and the Respondent ordered investigation into its affairs to adjudge whether there was any violation of the Stock Broker Regulations committed by it between January 2009 and August 2009. The impugned order was passed against the Appellant due to the fact that in synchronizing trades it acted both as a stock broker and a counter party broker.

The events due to which the show cause notice was issued occurred within a day and the volume of the scrips traded in respect of the following companies were noted:

- a. Winsome Textile Industries Limited (“**WTIL**”): 18 trades in scrips of WTIL worth 68% of the total number of shares traded on 19 March 2009.
- b. Aarey Drugs and Pharmaceuticals Limited (“**AADPL**”): 73 trades which amounted to 43.8% of the shares traded on 20 March 2009.

The Tribunal noted at the outset that the trades had been executed with an intent to increase trading and create artificial volumes of the shares. The Tribunal further noted that such

²⁴ SAT (2016).

misleading appearance of artificial volume in a particular scrip by giving the public the impression that a lot of trading activity is being conducted with respect to that scrip leads to deceive the public who then invest in such shares. Finally, the Tribunal noted that the Appellants were guilty because of the mere reason that their intention in executing the trades was to create an impression in the public that the scrips of the companies were a good source to invest in.

Conclusion: Intention is found depending upon circumstances of the case combined and may not exist independently. It seems from the analysis of the decisions that the intention enables to bring out the actual deception and synchronized trading in India. If the parties are innocent of this intention, then there will be no synchronized trading. However, it must not be lost track of that intention generally can also be inferred and does not require a direct and clear proof like most other matters.

5. Prevalent Market Conditions

This serves as a very important factor for the determination of synchronized trading. To be honest, it correctly points out the abnormality in the trades. This is because a synchronized trade stands differently from other trades which involve a particular movement in the market. It is the best for the regulatory authorities to identify and penalize such trades.

a) **Bhanwar Lal Paliwal v. Securities and Exchange Board of India**²⁵

Respondent had conducted investigation in the scrip of Asian Star Company Limited (“ASCL”) between the periods 10 October 2008 to 20 November 2008. It was through the impugned order that the Appellant had indulged in synchronized trading with a connected entity, namely Triveni Management Consultancy Services along with other brokers and clients belonging to the “Mehta Group”.

During the investigation period, the following details were noted:

- (i) **Volume of the scrips traded:** Out of the total 19,74,219 scrips traded by the Mehta Group along with the Appellant, 87.83% of the total volume were synchronized trades.
- (ii) **Price of the scrips traded:** The price of the scrips opened at Rupees 1,240 on 10 October 2008 and fell down to 1,101.55 on the same day and then rose to Rupees 1306.15 which was a 18.57% rise in 28 days when the Sensex had fallen by 19.73%.

The Tribunal noted with certainty that there were manipulations in the scrip of ASCL during the investigation period where there was an increase in volumes and price of scrip went up; but the SENSEX during the same period came down and there was no corporate announcement /

²⁵ SAT (2013).

sensitive news that could have caused upward price movement of scrip during IP. Therefore, it served as a clear indication that manipulation had existed when the entire market was down and there was nothing which could have been done in respect to raise the prices of the shares.

*b) Ketan Parekh v. SEBI*²⁶

The facts of this case have been covered under the fourth heading. In that case, the same will not be repeated here for the sake of brevity. The Tribunal noted in that case that Lupin's prices rose at a time when all the pharmaceutical company shares were progressing at a particular rate. It was through this rise in the prices that the Tribunal identified that there was synchronized trading in the shares of Lupin.

Conclusion: Market conditions play a determinative role in order to assess whether trading is synchronized but are guided by the beacons of price and volume. Similarly, the cases above denote that market conditions help in figuring out whether there is actual manipulation with an intent to deceive the public.

6. Effect of the trade on the market

This is the widest ground for consideration of whether a trade can be noted to be a synchronized trade or not. It involves an examination of the impact of the trade upon the market, which is important to view whether the trading in itself has harmed the market position or not.

*a) Gautam Jhaveri v. Adjudicating Officer, Securities and Exchange Board of India*²⁷

This appeal was against an order of the Respondent. The Respondent investigated the Appellant's trading in the scrips of Grishma Securities Pvt. Ltd. and noted through his order that the Appellant had executed structured and synchronized trades. The investigation noted that a total of 327 trades took place which were noted to be synchronized in nature. The Tribunal noted in this regard that the buyer and seller both punched the same price for the security into the system, as did the quantity of shares to be sold, and the moment at which the two orders were punched was nearly identical. There was a time differential of only one second which could not have been a mere co-incidence. It was noted that such trading "obviously interfere(s) with the true price discovery mechanism of the exchange" which causes a serious market irregularity. Therefore, the Appellant was pulled up for the effect that the trade would have on the true price discovery for the shares on the exchanges, especially the scrips which had been dealt with by the parties.

²⁶ SAT (2006).

²⁷ SAT (2007).

b) **Smt. Krupa Sanjay Soni v. SEBI**²⁸

The trading activity of Appellants and a few others in the scrip of Shree Global Tradefin Limited was investigated by the Respondent for the period 23 March 2009 to 20 November 2009. Through the impugned order, the Respondent recorded that the Appellants and its group had the highest concentration of trading in the scrip, and had accordingly dealt in the scrip in a fraudulent and manipulative manner.

During the investigation period, the price of the scrips traded rose from Rupees 325 to Rupees 428.5 which was an increase of 31.77% in a span of 163 trading days. The Tribunal noted that the trades were fictitious and there was no transfer of beneficial ownership in the shares from one entity to another. It was further noted that such trades are injurious to the market and result in creation of artificial volumes of the scrips. This specifically leads to a totally wrong signal to the members of the public who may invest in the hope of making some gains but ultimately land up with losses. Such trades executed by the Appellant and its related entities accounted for a total of 1.99% of the total market volume during the investigation period, therefore forming a large proportion of the market volume.

Conclusion: The effect of trade may be viewed upon the market through examination of its impact on the prevailing market conditions. In the cases aforementioned, this forms the primary determinant where the trades in themselves resulted in manipulation of the market, affecting large volumes of shares. Such trading if permitted may have a widespread adverse effect on the pricing of shares, and more than anything on the transparency of the screen-based stock trading that India takes pride in.

7. Repetitive and Constant Trading by Parties

The actions of related entities and group parties showcase a strong case for manipulation in the stock market. Such cases arise on the basis of the connection between the parties which result in a systematic manner of trading with a pre-conceived intent. Though the discovery of such mechanisms poses a great problem to regulatory agencies, it offers a very clear scope of determination of manipulative practices.

a) **Anita Dalal v. SEBI**²⁹

The Appellant was an individual investor and a trader in the securities market. The Respondent detected synchronized trading while investigating the dealings in the scrips of Temptation Foods Limited, Bang Overseas Limited and other entities. It was noted that a group of connected

²⁸ SAT (2014).

²⁹ SAT (2012).

clients indulged in synchronized trades in the scrips to create artificial volume. The Whole Time Member of the Respondent confirmed that the Appellant had been involved in the synchronized trading and subsequently passed the impugned order restraining the Respondent from accessing the markets for a span of 18 months. During investigation it was noted that out of the order quantity of 92596 on 10 March 2008, a total of 5000 shares got matched in the transaction with the counter party.

The Tribunal noted that during the period of investigation and even before and after the same there was a process of continuous, periodical and conscious matching in several trades over a period of time. It was noted that the Appellant was involved as a party with a group consistently which resulted in the synchronized trades in the market and contributed to the creation of artificial volumes. The prime important fact which made the Tribunal realize the amount of manipulation was the matching of 5000 trades out of a total of 92000 trades, not only on one occasion but repeatedly and consistently over a period of time.

b) In Re: Samurai Securities Private Limited³⁰

SEBI investigated in the shares of MIC Electronics listed at the BSE and the NSE. Through examination, it was discovered that Samurai Securities Private Limited engaged in self-trades in order to artificially inflate the volume of MIC's scrip, creating a false and misleading appearance of trading in the securities market. The SEBI order being summarized examines exactly that question.

Through the investigation, it was noted that:

- (i) **Volume of the scrips traded:** It was noted that 18,22,122 scrips of MIC were traded at the BSE while a total of 29,22,638 scrips were traded at the NSE.
- (ii) **Price of the scrips traded:** The price of the scrip increased from 8.59 on 17 February 2012 to Rupees 12.09 on 22 February 2012.

The Tribunal stated in this case that recurrent trading in illiquid scrips may imply that the broker was involved in the development of synchronized trading, which results in an unnatural increase in the price/value of the scrips. It is to be noted that the case found the broker liable for acting in an unreasonable manner and the failure to note with due care caution the involvement of its clients in such practices.

Conclusion: It is a determinative factor to understand synchronized trading though not an independent factor, and shall point towards a strong case. It has to be also noted as a side note

³⁰ SEBI (2017).

that the identification of such cases poses the greatest problems. In any case, the working of the regulatory agencies with the help of intuition and their electronic techniques may give them an edge in certain cases.

The examination of this concept has shown that it is very difficult in order to ascertain and point out a synchronized trade, without looking at the various related concepts. In that light, the next Part shall try to understand and figure out the reasons due to which such a situation exists and what can be done in that regard.

VI. CONCLUSION

The discussion in the previous Part focusses on the various aspects through which a trade may be considered to be a synchronized trade. This is a very detailed examination and involves numerous factors out of which many have been covered in the previous part. It has to be noted that the concept of synchronized trading is vague, undefined and its determination is at the mercy of the adjudicators. There seems to be no way to say that a particular trade will not be synchronized but certain general pointers in this regard have been established with the help of the previous Part. Connecting this aspect to the primary discussion under the topic of corporate crimes, it must be noted that this is a grave and an anonymous corporate crime which may lead to losses for millions and also disrupt entirely the way the market functions on a particular day in respect of a scrip. Such dangers need to be addressed by the regulatory authorities in order to bring about a change in the situation.

The definition of Sutherland from 1939 which covers white collar crime to be the crime done by persons of high social status and during occupation applies to the instance of synchronized trading. Most of these crimes are done by entities which are related and by brokers who are actually employed by such entities. Being a corporate crime, its redressal is insufficient in India as the large corporates get away with raising the prices of their shares, increasing volume of trading of their shares and even exiting the market at a profit with the help of synchronized trading. It causes unbearable loss to the normal traders and persons who do not have large means to survive themselves and their families. In that scenario this crime of synchronized trading which is punished by the provisions of various regulations has to be controlled.

However, like most white-collar crimes, it appears to have no identifiable victim and low visibility. It is only when the crime is detected that it becomes possible to apprehend a suspect. But even after the suspect is apprehended, the web of synchronized trading is so complex that it is nearly impossible to definitively prove the guilt of the person. This is also because most of these people are quite aware of how the game works and outsmart the regulators. Another

problem which arises is dummyming in respect of synchronized trading. Most of these activities are performed by persons on behalf of the top management of the company. Though these people actually performing the activities may be caught, the actual perpetrators always manage to get away as they do not form a formidable link with the top management. This factor prevents synchronized trading from being punished in a requisite manner.

The number of transactions over the stock exchange are overwhelming per day and it is nearly impossible to pick out one transaction and start analyzing the connected transactions in its regard. This is a problem which the regulators face. The employment of artificial intelligence devices which directly pull over suspicious cases of trading appears to be the need of the hour if such indiscriminate trading has to be stopped.

Finally, it has to be noted that the story is far from over. The already decided cases and the manner in which the criminals have been apprehended is testamentary to the fact that there is strong action being taken by the regulators. However, as they say criminals are always a step ahead. It is this point which has to be kept in mind and acted upon. It can only be hoped that the Indian regulatory agencies come up with a robust plan to cease such illegal and immoral activities, so that the Indian trading ecosystem does not suffer much damage.
