DABBA TRADING GOES ONLINE

"Crooks are getting smarter and technology is getting more advanced, and this makes the crook ahead of the police in the game"

The innovation of new technology not only allow to devise the new means of working and after each new advent of technology, it brings advance and easy to use mechanism and tools which allows entities a better control, methods of operation, utilization of human and other resources. But at the same time it allows the fraudster to also exploit these new mechanisms to commit frauds and other economic/cyber crimes. The main drawback is that by the time, the general public or investigation agencies becomes aware of these novel methods of committing fraud, the fraudster shift to further advance technology. Another drawback with the investigation agency is the availability of technology and knowledge of diversified fields and by the time they try to acquire these skills , it becomes outdated.

Dabba Trading" also known as "Bucketing" is the process used by brokers to route their client's trades outside the Stock/Commodity exchange. In such trading, the broker either does not execute any trade or matches and execute trades on its own terminal. "Dabba" has its origin in the developed markets where a system called bucketing prevails. Bucketing is an illegal practice where a stockbroker executes a customer's trade without taking it to a stock exchange with the hope of making some gains at a future date. essentially, bucketing involves the confirmation of an order from a client without actually executing the order on the client's behalf. The anticipation is that the broker will be able to realize enough profit to offset the difference to the client at a future date, either due to executing the order at a later date or through profits generated on other transactions.

The broking house that engages in this activity are called bucket shops. Dabba trading operates essentially like the American bucket shops of the 1920s that existed before the Securities and Exchange Commission (SEC) was set up.

The mechanics or Modus Operandi of Dabba Trading

- The "Dabba" means box and in modern context, a computer. A Dabba operator in the securities market's parlance is the trader/operator who executes "Dabba

Transactions". His office is the replica of any broker office having number of customers executing the trade on the terminals linked to the exchange showing market rates/trades.

- Earlier, the dabba trading do not execute the investor's trades on the stock exchange system but in the dabba operator's books only. A dabba operator acts as a principal to all the trades and not as an agent of the client. He is a counter party to the trades, whereas, he should be the Clearing Corporation who guarantees trades on the BOLT/NEAT system. This kind of operation, where trade is kept within the books of the operator is called "dabba" in the popular market terms.

- But now, the NSE & BSE has provided the facility for the investors to verify their trades on the NSE/BSE websites. This facility has made the broker vulnerable to be exposed to the investor's and can made him liable for civil & criminal remedy. In order to encounter such situation and to deceive the educated investors, the fraudster persons have developed novel and sophisticated mechanism of online dabba trading which even take care of all exchange procedures and rules and difficult to detect.

ONLINE DABBA TRADING :- This fraudulent practice is prevalent only in the F&O segments because the exchanges allows the modification of client codes in the F&O segments by the brokers at their choice without any security mechanism or supervision by the exchanges.

- The client places an order for buy or sells position on the exchange in the F&O segments. The trades is executed on the exchange and reported to the client.

- Within few second, the broker execute the reverse transaction where by the position of the client on the exchange becomes nil.

- Then the broker changes the client code of the reverse transaction into a different client code and thus the contract note is generated for the transaction done by the client only and even if the investor verify the transaction on the exchange, it will not show the reverse transaction in his client code as the client code has already been changed.

- Subsequently, when the client squares the transaction, the similar reverse transaction is executed and client code is changed.

- Thus, as the net position on both the dates of buying and selling is nil, the ultimate profit or loss accrued to the client vis-à-vis broker only.

- Normally, in such cases, the broker will not issue the contract notes and will report the transactions manually. Some will provide only the MTM bills that too just computer output on the plain paper without any stamp/letterhead so that these can not be used as evidence against them.

- The main risk to the investor is whenever, the broker suffer heavy losses due to risk they undertake due to dabba trading, they are likely to dispute the transactions or abscond. Most of the brokers who had absconded in last three years are due to losses suffered due to such frauds.

- Some of the fraudster have developed the software whereby , the moment transaction is executed in the client account, an automatic reverse transaction is executed so that these manipulation can be done at the large level because manually it required a number of people

In one of the cased investigated by the Economic Offences Wing of Delhi Police, this modus operandi was used by the broker to defraud various innocent investors. The broker used automated software whereby the reverse transactions were executed in the account of various transactions and subsequently the client code of the reverse transactions was changed within few seconds. Due to continuous rise in the share market over the period 2005 to 2007, the broker suffers heavy losses due to dabba trading. In order to escape the liabilities, the broker has not only regenerated the contract notes whereby includes the reverse transaction in the client bills because if the reverse transactions are included in the client account, no profit would accrue to the client as both the transactions have been done at the same time.

The fraudulent broker has gone to the extent of registering complaint against the innocent clients to whom, the profit has accrued due to such transactions on the ground that such investors have colluded with the respective Relationship Manger and changed the client code of the reverse transactions.

A large number of investors have filed the complaints with the exchanges as well as police but action was taken by the police in 4/5 cases only because of the following factors:-

- The broker being a large entity, having battery of lawyers and being financially sound stood at a bigger platform against whom a small investors found difficult to fight before the police as well as in the court.

- The investors are not aware of these technicalities and so not in a position to explain what actually went wrong while the brokers with the legal teams are able to manipulate the facts.

- The exchanges rather to take any action themselves and acting as goons for broker send the complaint to the broker for redressel. The redressel mechanism of the exchange is governed by the arbitrators who hardly has any knowledge of the mechanism of the exchange and not in a position of redress the grievances of the small investors.

- The exchanges and mechanism in the SEBI acting in a concerted manner have blocked all the remedies for the investors:-

1. The exchange never provide the detail of the transactions executed in the client account by the broker on the server of the client. The exchange as well as SEBI will only ask the broker to provide the detail of the transactions to the client . Thus the client can never obtain or access the information regarding the change of client code or unauthorized transactions executed in his account and thus suffer from the capacity to present his case before any forum.

2. The exchanges under the RTI act refused to provide the information to the client on the ground of inapplicability of RTI act to the exchanges. The CIC in a number of case directed the SEBI to provide the information but instead of providing the information, SEBI has challenged the order in the Bombay HIGH Court seeking exemption from providing the information on frivolous grounds.

3. Thus, the client has no choice in either way, neither it can proceed with civil remedy due to absence or access to the manipulations by the brokers not it can proceed with criminal as it being technical, the convincing to the police may be a Herculean task.

Neeraj Aarora
Cyber Lawyer