BEFORE THE ADJUDICATING OFFICER

SECURITIES AND EXCHANGE BOARD OF INDIA

[ADJUDICATION ORDER Ref No.: Order/ VV/AS/2021-22/14591]

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

In respect of:

Baid Mercantiles Limited
(PAN: AABCB0818R)
58, Elliot Road, 2nd Floor,
Kolkata - 700 016 (West Bengal)

In the matter of dealing in Illiquid Stock Options at 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 '**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.

2. The reversal trades are considered as non-genuine trades if it involves 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. 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. Baid Mercantiles Limited (hereinafter referred to as '**Noticee'**) was one of the several entities which were indulged in execution of such alleged non-genuine trades.

3. It was observed from the trade log that the Noticee had executed a total of 8 such trades in 2 unique contracts which allegedly led to creation of artificial volume of total 4,60,000 units. It is further observed that the Noticee, by executing non genuine trades during the relevant period, registered a negative close out difference of ₹23,00,000/- approx. The trades entered by the Noticee were reversed on the same day within a very short span of time 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. The summary of dealings of Noticee in such 2 Stock Options contracts is as follows:

Table 1 – 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	ACCL15APR1710.00CE	12.00	130000	2.00	130000	100%	100%	100%	100%
2	CESC15APR600.00CEW4	18.00	100000	8.00	100000	100%	100%	100%	100%

4. From the above table it was observed that: -
   a. The alleged non-genuine trades have contributed significantly when compared with the total number of trades from the market in the above contracts. The non-genuine trades of the Noticee: -
      i. were 100% of the total trades that had happened in the aforementioned contract; and
      ii. were 100% of the total trades of the Noticee that had happened in the aforementioned contract.
   b. The whole volume of 4,60,000 generated by the Noticee in all of the above contracts due to its non-genuine trades were artificial volume, and further this artificial volume, generated by the Noticee, also contributed significantly to the extent of 100% of the total volume in said contracts in the market.

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

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

5. Based on above findings of the investigation, 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 SEBI (Prohibition of Fraudulent and Unfair Trading Practices related to Securities Markets) Regulations, 2003 (hereinafter be referred to as, the "PFUTP Regulations") by the Noticee and appointed Shri Amit Pradhan, Chief General Manager as Adjudicating Officer ('**erstwhile AO**') vide *communication order* dated April 26, 2021 to inquire and adjudge under Rule 5 of SEBI (Procedure for Holding Inquiry and imposing penalties) Rules, 1995 (hereinafter be referred to as "**Adjudication Rules**") and under section 15HA of the SEBI Act, the alleged violations by the Noticee. Thereafter, vide *communication order* dated June 21, 2021, this case has been transferred to undersigned 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"*. The text of these provisions of PFUTP Regulations are as under:

PFUTP Regulations

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.

6. After receipt of records of these proceedings, the notice to show cause no. EAD – 9/ADJ/SCN/VKV/AKS/22819/2021 dated September 07, 2021 (hereinafter be referred to as '**SCN'**) issued to the Noticee in terms of Rule 4(1) of the Adjudication Rules read with section 15I of the SEBI Act calling upon it to show cause as to why an inquiry should not be held against it 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. The SCN was duly served upon the Noticee *via* Speed Post Acknowledgement Due ("**SPAD**") on September 13, 2021. After seeking extension to file the reply in the matter, vide letter dated October 26, 2021, the Noticee submitted his written submissions in the concerned matter. Accordingly, in the interest of principles of natural justice and on the basis of the Noticee's reply and the material available on record, an opportunity of hearing was granted to the Noticee in terms of Rule 4(3) of the Adjudicating Rules. On November 12, 2021, authorized representative of the Noticee *viz*. Mr. Anil Shah, Advocate appeared before me for hearing and made submissions on the basis of Noticee's reply dated October 26, 2021. Mr. Shah also made a request for a weeks' time to make additional written submissions in the matter and his request was acceded to. Thereafter, vide letter dated November 17, 2021, the Noticee submitted his additional written submissions in the concerned matter.

7. The replies/submissions of the Noticee made vide letters dated October 26, 2021 and November 17, 2021 and oral submissions made during hearing *inter alia* are as follows:

   a. The allegations made in and findings arrived at in the SCN as against the Noticee are misconceived and based on incomplete and incorrect assumption of facts. It denies each and every allegation and/or contention and/or observation made in the SCN and nothing therein stated should be deemed to have been admitted and/or inferred to have been admitted by it, save and except to the extent specifically admitted herein.

b. The Noticee denies that its dealings in the stock options can be termed as "*illiquid*", as wrongly contended in the SCN. It is further submitted that firstly, the SCN has failed to define the term "*illiquid*".

c. The investigation period pertains to the period from 01.04.2014 to 30.09.2015 and it is surprised to receive the SCN after 6 years there from, especially in the light of the fact that not a single warning/alert/alarm was raised, either by the BSE or by SEBI. It is most respectfully submitted that therefore, the SCN suffers from serious laches. Further, no satisfactory reasons or even a whisper is recorded in the SCN to explain or justify the delay in issuing the SCN. Thus, it is not in a position to recollect and explain the logic behind its trading decisions in each stock option, collate the data fully and offer clarification effectively. In this regard, the Noticee has placed reliance upon the judgement of the Hon'ble Securities Appellate Tribunal ("**SAT**") in the case of *Rajeev Bhanot* in Appeal No. 396/2018, *Rakesh Kathotia* in Appeal No. 07/2016 and *Ashok Rupani*, in Appeal No. 417/2018. Also the order and the findings of the Hon'ble SAT were upheld by the Hon'ble Apex Court in the Appeal preferred by SEBI in the matter of *Ashok Rupani (Supra)*. The Noticee has also placed reliance upon the Hon'ble Apex Court judgement in the matter of *Mansaram v. S.P. Pathak and Others* (Civil appeal No 1262 (N) of 1978) and 17 other judgements of Hon'ble Supreme Court and Hon'vle SAT on the question of delay.

d. The SCN is totally silent on the connection of parties, counter parties, broker and counterparty broker to its trades. The SCN assumes that there was meeting of mind on mere surmises and conjectures. There is no credible evidence to deduce meeting of minds between the counter party to the impugned trades and the Noticee. On connections and collusions, the Noticee has placed reliance upon the judgements of the Hon'ble SAT in the matter of *Nishith Shah HUF* (Appeal No. 97/2019), *Pine Animation* (Appeal No. 102/2020), *Labhu Gohil*, Appeal No. 26/2019, *Narendra Ganatra* (Appeal No. 47/2011), *Jagruti Securities vs SEBI* [2008 SCC Online SAT 184: 2008 SAT 184], *S.P.J. Stock Brokers Pvt. Ltd. vs SEBI* [2013 SCC OnLine SAT 67: [2013] SAT 17] and *HB Stockholdings Limited vs SEBI* [2013 SCC OnLine SAT 56: [2013] SAT 44].

e. The decision to sell within short span of time at different price; without any corresponding charge of collusion ought not to be held against the Noticee. Thus, the SCN ought to be set aside for the sole reason that neither any credible evidence is relied upon nor placed on records. The counterparty could have been same because the trade was done within fraction of seconds itself so maybe on online platform, the same counterparty was accepted by the system/obviously it could have matched with other party too, one cannot be certain about the probability of trades matching with other parties. It will be logical to assume and conclude that only brokers are in position to match alleged trades with counter party brokers and it was impossible for the Noticee as an individual entity to enter into alleged matching of trades.

f. The buy and sell rates should have been compared on the basis of notional values, instead of the premium. It may be appreciated that the notional value represents the total underlying amount of the derivative, which is much larger than the market value of contracts. We further state that the volume of derivatives was very small vis-à-vis the volume of underlying securities and therefore, such a small volume is not sufficient to create any kind of artificial volume. The Noticee have merely executed two contract of 8 trades for 4,60,000 units which is 0.0027% of the total trades of the investigation period, which could never tantamount to execution of non-genuine reversal of trades.

g. The Noticee neither aware, nor involved nor have participated nor have means to verify and comment on trades of other entities, who were apparently counter parties to its trades. Squaring off of its trades with a difference in values were based on its understanding of the market and hence, could not have led to generation of artificial volumes, as wrongly alleged. It denies that these trades are non-genuine in nature and have resulted in generating artificial volumes just because the trades were reversed on the same day with same counterparties at a substantial price difference without any basis for significant change in the contract price. The said allegations are based merely on presumptions and assumptions and therefore, are totally baseless.

h. In terms of Clauses 1.2 and 1.3 of Risk Disclosure Document (RDD), which deals with risk of low liquidity and risk of wider spread, it can be safely concluded that SEBI is well aware of the possibility of trades being executed at substantial price difference and possible loss due to lower liquidity and wider spreads in illiquid stock options. The SCN also records that the contracts in which we have dealt were illiquid. It is not disputed that liquidity in the contracts recorded in the SCN was low and hence, spreads were bound to be wide so we were constrained to square off our trades at a price difference, which is also well appreciated and accepted by the RDD issued by SEBI.

i. The Noticee trades have been settled in terms of the BSE and the resultant profit has been offered for tax in our return of income for AY 2015/2016.

j. BSE and SEBI have themselves allowed and permitted trading in options for far months with a strike price which are at large variance to current market price. Further, Stock Exchanges regularly come out with list of illiquid scrips in cash segment, however no such list is issued by exchanges or regulators for dealing in stock options contracts. Also, merely because on-line preventive measure and checks and balances did not exist with the regulator at the relevant time to avoid inadvertent reversal trades no adverse inference be drawn against the Noticee and thus, to fasten responsibility or allege a single investor is unwarranted.

k. Derivative market is 'zero sum game' and thus in each and every case one party will inevitably make profit and counterparty will make loss. Thus, profit and loss is concomitant to trading in derivative segment.

l. There was no major movement in price of underlying scrip which itself proves that its trades had no impact on market. Further, it had traded on a very little period during the investigation period. Its trades had neither distorted the equilibrium in market nor could have caused any loss or prejudice to the investors at large.

m. In view of aforesaid submissions, the Noticee requested to drop the present proceedings *qua* the Noticee.

8. I have considered the allegation levelled in the SCN, reply / submissions of the Noticee and the relevant material brought on record. From the reply of the Noticee, I note that the Noticee has not disputed the execution and subsequent reversal trades as alleged in the SCN. However, the Noticee has raised technical objection of delay in issuance of SCN after 6 years of the impugned transactions and stated that due to the delay it is not in a position to recollect and explain the logic behind its trading decisions in each stock option, collate the data fully and offer clarification effectively. In this regard, I note that the impugned transactions belong to March 25, 2015, wherein the investigation period is April 01, 2014 to September 30, 2015. I further note that an extensive investigation in this case had been initiated by SEBI upon observing large scale reversal of trades in stock options segment of BSE leading to creation of artificial volume during investigation period. Due to elaborate and extensive investigation

process such as - co-ordination with concerned stock exchange in respect of a large number of entities (involving more than 14,000 entities), complexity and extensive analysis of the data/ information, etc., in this case, the final investigation report submission has taken time. Thereafter, SEBI came out with a Settlement Scheme (hereinafter referred to as "Scheme") in terms of Regulation 26 of SEBI (Settlement Proceedings) Regulations 2018 in the concerned matter, wherein one-time opportunities were provided to the the entities including the Noticee against whom adjudication proceedings were approved for involvement in generation of artificial volumes. SEBI issued a public notice dated July 27, 2020 about the launching of the aforesaid Scheme and the modalities for availing the benefit of the Scheme. The public notice was also made available on the website of the BSE. In addition to the same, all the entities including the Noticee were intimated through email and letters. In terms of the scheme, any entity desirous of availing the benefit of the scheme could avail the same by filling up the respective requisite details and paying the applicable settlement amount through the online platform made available on SEBI's website. However, the Noticee has not availed the aforesaid scheme of SEBI. Thereafter, vide communique dated April 26, 2021 the erstwhile AO was appointed as the Adjudicating Officer in the instant proceedings, however, pursuant to his deputation, this case has been transferred to me and Thereafter, on receipt of records, the SCN to the Noticee has been issued on September 07, 2021, informing the Noticee about the detailed charges/allegations against it. In this regard, I note that, initiating a proceeding under the appropriate provisions of SEBI Act is a regulatory prerogative of SEBI depending upon the outcome of the fact finding exercise, which is the investigation done in this case, and just because the alleged violation was committed in a distant past cannot be a ground to vitiate initiation of these proceedings.

9. The Noticee has placed reliance upon various judgements of Hon'ble SAT and Hon'ble Supreme Court on the question of delay. In this regard, I note that there is no provision in the SEBI Act which lays down any limitation period for initiating any proceedings/ action under the SEBI Act. For establishing the delay, if any, in the matter, the date when the violation came to the notice of the SEBI would be the relevant point and not the date of violation. Whether a delay in a particular case is justified or not depends on the facts and circumstances of each case. I have perused the judgement of *Rajeev Bhanot* (*Supra*), *Rakesh Kathotia* (*Supra*) and *Ashok Rupani (Supra)*, and I note that the facts of these cases can be easily distinguished from the instant matter, as charge in this case relates to a fraudulent act of non-genuine trades executed by the Noticee in illiquid stock options. I have also perused the

Hon'ble Supreme Court order dated November 15, 2019 dismissing the SEBI appeal in *Ashok Rupani (Supra)* and I note that in the said order the Apex court has left the question of law open. I have further perused the Hon'ble Supreme Court order pronounced in the matter of *Mansaram (Supra)* and 17 other orders relied upon by the Noticee on delay and exercising power within a reasonable time and I note that the decisions in these judgements, also endorses to the legal position regarding the delay, as stated above. Further, in the case of *Ravi Mohan & Ors. Vs. SEBI (SAT Appeal No. 97 of 2014 decided on 16.12.2015)*, Hon'ble SAT while referring to its own decision in *HB Stock Holdings case* (*supra*) and decision of Hon'ble Supreme Court in the matter of *Collector of Central Excise, New Delhi vs. Bhagsons Paint Industry (India) reported in 2003 (158) ELT 129 (S.C.),* held as follows:

> *"...Based on decision of this Tribunal in case of HB Stockholdings Ltd. vs. SEBI (Appeal no. 114 of 2012 decided on 27.08.2013) it is contended on behalf of the appellants that in view of the delay of more than 8 years in issuing the show cause notice, the impugned order is liable to be quashed and set aside. There is no merit in this contention, because, this Tribunal while setting aside the decision of SEBI on merits has clearly held in para 20 of the order, that delay itself may not be fatal in each and every case. Moreover, the Apex Court in case of Collector of Central Excise, New Delhi vs. Bhagsons Paint Industry (India) reported in 2003 (158) ELT 129 (S.C) has held that if there no statutory bar for adjudicating the matter beyond a particular date, the Tribunal cannot set aside the adjudication order merely on the ground that the adjudication order is passed after a lapse of several years from the date of issuing notice………………"*

10. I further observe that, the Hon'ble SAT in the matter of *Ashlesh Gunvantbhai Shah Vs SEBI (*Appeal No. 169 of 2019 Date of Decision: 31.01.2020) made the following pertinent remarks:

> *"It is no doubt true that no period of limitation is prescribed in the Act or the Regulations for issuance of a show cause notice or for completion of the adjudication proceedings. The Supreme Court in Government of India vs, Citedal Fine Pharmaceuticals, Madras and Others, [AIR (1989) SC 1771] held that in the absence of any period of limitation, the authority is required to exercise its powers within a reasonable period. What would be the reasonable period would depend on the facts of each case and that no hard and fast rule can be laid down in this regard as the determination of this question would depend on the facts of each case. This proposition of law has been consistently reiterated by the Supreme Court [..].*

11. I also note that, the Supreme Court recently in the case of Adjudicating Officer, *SEBI vs. Bhavesh Pabari (2019) SCC Online SC 294* held:

> *"There are judgments which hold that when the period of limitation is not prescribed, such power must be exercised within a reasonable time. What would be reasonable time, would depend upon the facts and*

circumstances of the case, nature of the default/statute, prejudice caused, whether the third-party rights had been created etc."

12. I am also of a view that, Hon'ble SAT has qualified the aforesaid ruling by saying that the reasonable period would depend on the facts and circumstances of each case and that no hard and fast rule can be laid down in this regard. In my view the present proceedings do not suffer from any infirmity on the ground of delay. I, therefore, hold that there is no protracted delay as contended and hence, the contention of the Noticees in this regard is rejected.

13. Coming to the merit of allegation, it is worth mentioning that reversal trades are considered non-genuine 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. Admittedly, the Noticee had indulged in 8 such reversal trades in 2 unique contracts during the Investigation Period involving reversal of trades with same entity with whom it had done buy/ sell transaction, in short span of time, respectively, in a synchronized manner. It is noted from the trade log relied upon in the matter that the Noticee and counterparty (ies) both had placed their respective sell-buy and buy–sell orders in same time i.e. within few milliseconds. Further, each trade involved matching of time, price and quantity of units. For example, in respect of the 4 trades in contract "CESC15APR600.00CEW4" dated March 25, 2015. The trades of the Noticee are detailed in the following table:

Table 2: Trades of the Noticee in the contract of "CESC15APR600.00CEW4"

Sl.	Date	Buyer	Seller	Buy Order Time	Sell Order Time	Trade Time	Trade Rate (Rs.)	Trade Quantity
1	25/03/15	Abhishek Agarwal HUF	Baid Mercantiles Limited	12:56:54	12:56:54	12:56:54	8.00	50000
2	25/03/15	Baid Mercantiles Limited	Abhishek Agarwal HUF	12:56:57	12:56:57	12:56:57	18.00	50000
3	25/03/15	Abhishek Agarwal HUF	Baid Mercantiles Limited	12:57:22	12:57:22	12:57:22	8.00	50000
4	25/03/15	Baid Mercantiles Limited	Abhishek Agarwal HUF	12:57:26	12:57:26	12:57:26	18.00	50000
		Total						**2,00,000**

14. It is observed from the above table that –

    a. The Noticee, at 12:56:54 hrs placed a sell order for 50,000 units of call option of contract "CESC15APR600.00CEW4" at a price of Rs. 8.00 and 50,000 units of this sell order of the Noticee got matched with the buy order of another entity namely, Mr. Abhishek Agarwal HUF, which himself had placed a buy order for 50,000 units in the same contract at 12:56:54 hrs i.e. few milliseconds earlier of the sell order placed by the Noticee.

    b. Thereafter, the Noticee, at 12:56:57 hrs placed a buy order for 50,000 units of call option of contract "CESC15APR600.00CEW4" at a price of Rs. 18.00. This buy order of the Noticee got matched with the sell order of Mr. Abhishek Agarwal HUF, which himself had placed a sell order for 50,000 units in the same contract at 12:56:57 hrs i.e. few milliseconds earlier of the buy order placed by the Noticee.

    c. In similar pattern, the Noticee, at 12:57:22 hrs placed another sell order for 50,000 units of call option of contract "CESC15APR600.00CEW4" at a price of Rs. 8.00 and 50,000 units of this sell order of the Noticee got matched with the buy order of another entity namely, Mr. Abhishek Agarwal HUF, which himself had placed a buy order for 50,000 units in the same contract at 12:57:22 hrs i.e. few milliseconds earlier of the sell order placed by the Noticee.

    d. Thereafter, the Noticee, at 12:57:26 hrs placed another buy order for 50,000 units of call option of contract "CESC15APR600.00CEW4" at a price of Rs. 18.00. This buy order of the Noticee got matched with the sell order of Mr. Abhishek Agarwal HUF, which himself had placed a sell order for 50,000 units in the same contract at 12:57:26 hrs i.e. few milliseconds earlier of the buy order placed by the Noticee.

    <u>Observation:</u> Thus in the first instance the sell order placed by the Noticee at Rs. 8.00 was reversed with the same counterparty at Rs. 18.00, within 3 seconds in the same contract on the same day and in second instance the sell order placed by the Noticee at Rs. 8.00 was reversed with the same counterparty at Rs. 18.00, within 4 seconds in the same contract on the same day. The artificial volume generated through such 4 non-genuine trades was for 2,00,000 units of the said contract.

15. Similar pattern on trading was observed in respect of other 4 trades executed by the Noticee in other illiquid Stock Option contract, wherein trades were reversed in short span of time and buy-sell or sell-buy orders were placed within a time gap of few milliseconds. The buy

orders placed by the Noticee were matched with sell orders of counterparties and sell orders placed by the Noticee were matched with buy orders of counterparties in terms of number of units and price and time. Thus, the total volume generated through such non genuine trades was 4,60,000 units of the 2 Stock Options contracts. Such reversal of trades in quick succession with substantial price difference indicate towards employing of a manipulative device in connection with its dealing in said illiquid Stock Options contracts.

16. The Noticee has contended that, the SCN has failed to define the term "*illiquid*" and its dealings in the stock options cannot be termed as "*illiquid*". In this regard, I note that the term "*illiquid*" is antonym of "*liquid*" and in securities market it is used for "*a scarcely traded securities*". Therefore, an option contract that cannot be easily sold or converted to cash quickly at the prevailing market price will always be treated as "*illiquid*" option that has very low or no open interest. I further note that in its reply the Noticee has *inter alia* mentioned that *"…it is not disputed that liquidity in the contracts recorded in the SCN was low…"*. In view of the same, I found that the Noticee was well aware that the option contract in which it was trading was "*illiquid*" and therefore, I reject such contentions of the Noticee.

17. The Noticee has further contended that buy and sell rates should have been compared on the basis of notional values, instead of the premium. It may be appreciated that the notional value represents the total underlying amount of the derivative, which is much larger than the market value of contracts. In this regard, I note that an option is traded at market price in derivative market, which is a fraction of the notional value. Further, market price is calculated/ dependent on the "*supply and demand*" factors of a securities market. Therefore, market price of a security is a price agreed by buyers and sellers in the securities market. In the instant case, the stock options have been sold and bought at "market price" and therefore, it is relevant to consider the substantial difference in "market price" into consideration w.r.t. impugned trades while determining the nature of trades executed by the Noticee. In view of same, I found the contention of the Noticee not tenable.

18. The Noticee has contended that it had traded in stock options on anonymous and electronic trading platform of stock exchange and the SCN is totally silent on the connection of parties, counter parties, broker and counterparty broker to its trades. Further, the Noticee contended that the SCN assumes that there was meeting of mind on mere surmises and conjectures. There is no credible evidence to deduce meeting of minds between the counter party to the

impugned trades and the Noticee. I am of the view that the transactions in a particular contract were reversed with the same counterparties indicates a prior meeting of mind with a view to execute the reversal trades at a pre-determined price. Since these trades were done in illiquid option contracts, there was no trading in the said contract and hence, there was no price discovery in the strictest terms. The wide variation in prices of the said contracts, within a short span of time, is a clear indication that there was pre-determination in the prices by the counterparties while executing the trades. Thus, it is observed that Noticee had indulged in reversal trades with it counter parties in the stock options segment of BSE and the same were non-genuine trades. Therefore, the Noticee's contentions are not acceptable and hence rejected.

19. I further note that 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 its 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. Such transactions in illiquid Stock Options cannot be taken as genuine one. Such trading was apparently without any economic rationale. Thus, the Noticee claim of having no connection or prior meeting of mind or any specific role in creating artificial volume through alleged trades is not acceptable.

20. Further, with regard to the reversal trades carried out by the Noticee, I note that the Hon'ble Supreme Court in the matter of *SEBI vs. Rakhi Trading Private Ltd.*, in Civil appeals no., 1969 of 2011 with Civil Appeal Nos., 31743177 of 2011 and Civil Appeal No., 3180 of 2011 decided on February 8, 2018 had observed that *"the price discovery system itself was affected by synchronization and rapid reverse trade, which also had the impact of excluding other investors from participating in the market. The Supreme Court, therefore found that the traders having engaged in a fraudulent and unfair trade practice while dealing in securities, are hence liable to be proceeded against for violation of Regulations 3(a), 4(1) and 4(2)(a) of PFUTP Regulations"*.

21. With regard to reversal transactions, Hon'ble Supreme Court in the matter of *SEBI v Rakhi Trading Private Limited (Supra)*, further held that - "*Considering the reversal transactions, quantity, price and time and sale, parties being persistent in number of such trade transactions with huge price variations, it will be too 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*". In view of said Hon'ble Supreme Court judgment, I see no reason to take a different view in the present case. In view of the foregoing, I hold that the Noticee had indulged in execution of reversal trades in Stock Options with same counterparty (ies) on the same day, which are non-genuine in nature and have created false or misleading appearance of trading in terms of artificial volumes.

22. The Noticee has contended that counterparty could have been same because the trade was done within fraction of seconds itself so maybe on online platform, the same counterparty was accepted by the system/obviously it could have matched with other party too, one cannot be certain about the probability of trades matching with other parties. I note that, it is not mere coincidence that the Noticee could match its trades with the same counterparty with whom it had undertaken first leg of the respective trades. I further note that though direct evidence is not available in the present matter as regards to meeting of minds or collusion of the Noticee with other entities. The genuineness of trading has to be determined based upon circumstantial evidence involving multiple factors such as trading pattern, liquidity and volatility in the scrip /contract, etc. In this context, the Hon'ble SAT vide its order dated July 14, 2006, in the case of Ketan Parekh vs. SEBI (Appeal no. 2/2004) observed 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."*

23. Further, in *SEBI v Kishore R Ajmera (AIR 2016 SC 1079)*, Hon'ble Supreme Court held that - "*…in the absence of direct proof of meeting of minds elsewhere in synchronized transactions, the test should be one of preponderance of probabilities as far as adjudication of civil liability arising out of the violation of the Act or provision of the Regulations is concerned. The conclusion has to be gathered from various circumstances like that volume of the trade effected; the period of persistence in trading in the particular scrip; the particulars of the buy and sell orders, namely, the volume thereof; the proximity of time between the two and such other relevant factors. The illustrations are not exhaustive...*". The Hon'ble Supreme Court further observed

that – "*It is a fundamental principle of law that proof of an allegation levelled against a person may be in the form of direct substantive evidence or, as in many cases, such proof may have to be inferred by a logical process of reasoning from the totality of the attending facts and circumstances surrounding the allegations/charges made and levelled. While direct evidence is a more certain basis to come to a conclusion, yet, in the absence thereof the Courts cannot be helpless. It is the judicial duty to take note of the immediate and proximate facts and circumstances surrounding the events on which the charges/allegations are founded and to reach what would appear to the Court to be a reasonable conclusion therefrom. The test would always be that what inferential process that a reasonable/prudent man would adopt to arrive at a conclusion.*"

24. The trading pattern as found in this case in illiquid Stock Options cannot occur just by accident or coincidence. The trading behavior of the Noticee in this case makes it clear that aforesaid trades of the Noticee could not have been possible without prior meeting of minds. The synchronized trading by the Noticee 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 contracts in question. In view of the fact that these options contracts were illiquid in nature, having very small volume in trading, the Noticee created artificial volumes in Stock Options which was manipulative and deceptive in nature. Once the Noticee has been found to have indulged in such reversal transactions in illiquid Stock Options it is liable for its acts and omissions. Thus, I reject such contentions of the Noticee.

25. Considering the aforesaid facts and circumstances, I am of a view that the Noticee's reliance upon the judgements of the Hon'ble SAT in the matter of *Nishith Shah HUF* (Appeal No. 97/2019), *Pine Animation* (Appeal No. 102/2020), *Labhu Gohil*, Appeal No. 26/2019, *Narendra Ganatra* (Appeal No. 47/2011), *Jagruti Securities vs SEBI* [2008 SCC Online SAT 184: 2008 SAT 184], *S.P.J. Stock Brokers Pvt. Ltd. vs SEBI* [2013 SCC OnLine SAT 67: [2013] SAT 17] and *HB Stockholdings Limited vs SEBI* [2013 SCC OnLine SAT 56: [2013] SAT 44] on the question of connection and collusions is of no help to it on the basis of distinguished facts and circumstances. In view of the fact that these options contracts were illiquid in nature, having very small volume in trading, the Noticee created artificial volumes in Stock Options which was manipulative and deceptive in nature. Once the Noticee has been found to have

indulged in such reversal transactions in illiquid Stock Options it is liable for its acts and omissions.

26. The Noticee has contended that the derivative market is '*zero sum game*' and thus in each and every case one party will inevitably make profit and counterparty will make loss. Thus, profit and loss is concomitant to trading in derivative segment. I note that, it is not a case, where any of the parties of the trades executed by the Noticee were for intentionally booking any profit or loss. Further, this case is not dependent on loss or profit made by the entity and rather it deals with the impact of these non-genuine reversal of trades between the counter parties, which creates false or misleading appearance of trading. Further, the charge of artificial volumes created by the two counterparties by entering into non-genuine reversal of trade, is not dependent on making of loss or profit by an entity. Considering the same, I find no merit in such contentions of the Noticee.

27. The Noticee has further contended that it had traded on a very little period during the investigation period and its trades had neither distorted the equilibrium in market nor could have caused any loss or prejudice to the investors at large. In this regard, I note 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, hence, it would be appropriate to consider the impact of these transactions between the counterparties in totality. I found that all the 8 trades of the Noticees in two contracts were 100% of the total trades that had taken place in the impugned contracts and these impugned trades has contributed significantly to the extent of 100% of the total volume in said contracts in the market. I further note that these trades were part of the 81% (approx..) non-genuine trades executed on Stock Options Segment of BSE during the investigation period and when seen in totality these non-genuine trades have the ingredient to distort the equilibrium in market. I also note that, law does not allow any allowance for such fraudulent act of creation of misleading appearance of trading due to impugned reversal trades. In view of the same, I find no merit in such contentions of the Noticee.

28. The Noticee has submitted that its trades have been settled in terms of the BSE and the resultant profit has been offered for tax in our return of income for AY 2015/2016. Further, Also, merely because on-line preventive measure and checks and balances did not exist with the regulator at the relevant time to avoid inadvertent reversal trades no adverse inference be drawn against the Noticee. In this regard, I note that the Hon'ble Supreme Court in *Rakhi*

Trading (supra) case held that such undesirable transactions would certainly include unfair practices in trade and thus, orchestrated trades are a misuse of the market mechanism. The Hon'ble Supreme Court further observed that - "*The non-genuineness of these transactions is evident from the fact that there was no commercial basis to suddenly, within a matter of minutes, reverse a transaction when the value of the underlying had not undergone any significant change*". Thus, the Noticee's contention regarding non availability of on-line preventive measure and checks and balances from BSE and SEBU is devoid of any merit and rejected hereby. I further note that paying of taxes for earnings made through non-genuine reversal trades does not legitimate the impugned trades and in no way provide an authenticity to the genuineness of a trade. In this case, the Noticee has been charged for executing non genuine trades in illiquid stock options at BSE and creating artificial volume through such trades and therefore, such contentions of the Noticees are not tenable.

29. In terms of foregoing findings, I further note that the trading pattern of the Noticee in terms of volume of reversal trades, proximity of buy/sell and subsequent reversal evidences the indulgence, clearly demonstrates the manipulative practice by the Noticee by using the stock exchange platform to carry out non-genuine trades with the aim to execute such trades for various manipulative purposes. I note that the Hon'ble Supreme Court in the matter of *SEBI vs. Rakhi Trading Private Ltd.* (*supra*), also held that - *"The platform of the stock exchange has been used for a non-genuine trade. Trading is always with the aim to make profits. But if one party consistently makes loss and that too in pre-planned and rapid reverse trades, it is not genuine; it is an unfair trade practice". "The stock market is not a platform for any fraudulent or unfair trade practice. The field is open to all the investors. By synchronization and rapid reverse trade, as has been carried out by the traders in the instant case, the price discovery system itself is affected. Except the parties who have pre-fixed the price nobody is in the position to participate in the trade. It also has an adverse impact on the fairness, integrity and transparency of the stock market."*

30. In totality of the circumstances as observed above it is not acceptable that the Noticee has not employed any manipulative and deceptive device in contravention of the SEBI Act or the rules and the regulations made there under. Further, the non-genuine and deceptive trades as found in this case are covered under the definition of '*fraud*' and dealing of Noticee were '*fraudulent*' as defined under Regulation 2(1)(c) of the PFUTP Regulations.

31. In view of the aforesaid facts and circumstances, it cannot be ignored that synchronization of trades in pre-determined manner as found in this case had an adverse impact on the

fairness, integrity and transparency in the securities market. 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."

32. 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;*

33. Having regard to the factors listed in section 15J, it is noted that 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 2 Stock Option contracts which resulted into artificial volume of 100% generated out of the 8 non-genuine trades of the Noticee, I am of the view that such trades had created a misleading appearance of trading in the scrip. In these circumstance, I am of the view that for the market abuse and fraudulent practices by the Noticee monetary penalty needs to be imposed under section 15HA of the SEBI Act.

34. Taking into consideration all the facts and circumstances of the case including the aforesaid 15J 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) upon **Baid Mercantiles Limited** under section 15HA of the SEBI Act. In my view, the said penalty is commensurate with the violation committed by the Noticee in this case.

35. The Noticee shall remit / pay the said amount of penalty within 45 days of receipt of this order in either of the way of demand draft in favour of "*SEBI - Penalties Remittable to Government of India*", payable at Mumbai, or by following the path at SEBI website www.sebi.gov.in, ENFORCEMENT > Orders > Orders of AO > PAY NOW; OR by using the web link https://siportal.sebi.gov.in/intermediary/AOPaymentGateway.html. In case of any difficulties in payment of penalties, the Noticees may contact the support at portalhelp@sebi.gov.in

36. The Demand Draft or details and confirmation of e-payment made in the format as given in table below shall 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 'Payer/Noticee'	
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)	

37. 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.

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

Date: December 28, 2021
Place: Mumbai

Vijayant Kumar Verma
Adjudicating Officer