(2021) 06 SEBI CK 0181

In the Securities Appellate Tribunal Mumbai

Case No : Appeal No. 389 Of 2021

Prafull Anubhai Shah APPELLANT

Vs

Securities And Exchange Board Of India RESPONDENT

Date of Decision : 28-06-2021

Acts Referred:

Code Of Civil Procedure, 1908 — Order 41 Rule 27
Securities And Exchange Board Of India (Prohibition Of Fraudulent And Unfair Trade Practices Relating To Securities Market) Regulations, 2003 — Regulation 3, 4
Securities And Exchange Board Of India Act, 1992 — Section 12A

Citation : (2021) 06 SEBI CK 0181

Hon'ble Judges : Tarun Agarwala, Presiding Officer;M. T. Joshi, J

Bench : Division Bench

Advocate : Yugandhara Khanwilkar, Aishwarya Shubhangi, Abhiraj Arora, Rashi Dalmia, Karthik Narayan

Final Decision : ?Allowed

Judgement

Tarun Agarwala, Presiding Officer

1. The present appeal has been filed by the appellant against the order dated February 8, 2021 passed by the Whole Time Member (â??WTMâ? for

short) of the Securities and Exchange Board of India (â??SEBIâ? for short) debarring the appellant from accessing the securities market for a period

of one year for violating Section 12A of the Securities and Exchange Board of India Act, 1992 and Regulation 3 and 4 of the SEBI (Prohibition of

Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (â??PFUTP Regulationsâ?? for short).

2. The facts leading to the filing of the present appeals is, that the board of directors of the Company known as â??Soma Textiles and Industries

Limitedâ? (â??the Companyâ? for short) passed a resolution dated July 27, 2006 for issuance of Global Depository Receipts (â??GDRsâ? for short).

The board of directors also resolved in this resolution to open an account with Banco Efisa, S.A. (â??Bancoâ? for short), a bank based in Lisbon,

Portugal for the purpose of deposit of the GDR proceeds and to use the proceeds as security in connection with a loan. The resolution also authorized

one Mr. Sunil Patel as the authorized signatory to sign relevant documents on behalf of the Company. Based on this resolution the Company issued

18,50,000 GDRs for USD 17.2975 million wherein each GDR represented 10 equity shares of the Company.

3. Investigation in the issuance of the GDR revealed that the GDR was not issued with a proper consideration and without making adequate disclosure

under the Listing Agreement. Accordingly, a show cause notice was issued on July 21, 2017 alleging that Whiteview Trading Corporation

(â??Whiteviewâ? for short) was the only entity who subscribed to 1.85 million GDRs amounting USD 17.29 million and that the subscription amount

was paid by Whiteview by obtaining a loan under a loan agreement with Banco wherein the bank agreed to lend USD 18.5 million to Whiteview. This

loan was secured to account charge agreement with Banco by the Company. It was alleged that the account charge agreement was an integral part

of the loan agreement dated October 18, 2006 which allowed Whiteview to avail the loan in order to subscribe to the GDR issue which was

fraudulent. Further, the loan agreement as well as the account charge agreement was not disclosed to the Stock Exchange.

4. The only charge against the appellant was that he was a Director and was part of the resolution dated July 27, 2006 by which the first resolution

was passed by the Board of Directors for issuance of the GDR and for opening an account with Banco.

5. Before the WTM the appellant contended that he was appointed as non executive non promoter independent director with effect from January 24,

2004 and resigned on May 30, 2009. It was contended that he was never involved in the day-to-day affairs of the Company nor was part of any

decision making process relating to the GDR issue. The appellant further contended that he has not signed any agreement with any entity involved in

the alleged fraud and that his role as a non executive non promoter independent director was very limited and restricted. The appellant contended that he had no specific role in the GDR issue other than fact that he was present in the meeting of the Board of Directors when the resolution dated July

27, 2006 was passed for issuance of the GDR.

6. The WTM after considering the replies of the Company and other directors came to the conclusion that the issuance of GDR was a fraud played

upon the investors and this scheme was wrongly utilized in the securities market which was violative of Section 12A of the SEBI Act and Regulation 3

and 4 of the PFUTP Regulations. The WTM found that Whiteview was the only subscriber and a false impression was given to the shareholders and

investors that the GDR issue was subscribed by many entities. It was contended that the way the loan was obtained by Whiteview from Banco which

was secured by a account charge agreement given by the Company was fraudulent and that the loan agreement as well as the charge agreement was

never disclosed to the Stock Exchange and therefore violative of Clause 49 of the Listing Agreement. Accordingly, directions were issued against the

Company as well as against the appellant.

7. Insofar as the appellant is concerned, no finding whatsoever has been given as to whether the appellant had any role to play in the issuance of the

GDR. The only finding given in paragraph 48 of the impugned order is a finding of a general nature, namely, that the Board of Directors plays a key

role in balancing the interests of managements and shareholders and that the directors are required to ensure fairness and transparency in the dealings

of the Company. It was also indicated by the WTM in the same paragraph that if an act or omission occurs through board processes then directors

including such non-executive directors can be held liable. The WTM thereafter concluded that since the appellant had participated in the resolution of

the Board of Directors, he did not act diligently and since he was aware of the authorization of the pledge agreement executed by the Company the

WTM concluded that such execution of the pledge agreement should have been objected by the appellant which he did not do so and accordingly

issued an order debarring the appellant from accessing the securities market.

8. We have heard Ms. Yugandhara Khanwilkar along with Ms. Aishwarya Shubhangi, the learned counsel for the Appellant and Mr. Abhiraj Arora

along with Ms. Rashi Dalmia and Mr. Karthik Narayan, the learned counsel for the respondent.

9. In our opinion, the impugned order insofar as the appellant is concerned cannot be sustained in the light of the various decisions given by us relating

to the GDR issue. In Adi Cooper vs. Securities and Exchange Board of India (Appeal No. 124 of 2019 decided on November 5, 2019) this Tribunal on

an almost identical issue wherein the resolution of the Board of Directors for opening an account was verbatim to the present resolution. The modus

operandi was also the same. The Tribunal after analyzing held that:-

Â â??8. The finding of the WTM against the appellant Adi Cooper is wholly misconceived, farfetched and cannot be accepted to come to a

conclusion that the said appellant was party to a resolution which had an intention to manipulate the market or defeat its mechanism. Admittedly, the

appellant Adi Cooper was party to a resolution of the Board of Directors dated January 30, 2008 which only resolved the company to open an account

with the EURAM bank for the purpose of deposit of the GDR proceeds. The resolution further authorized the bank to use the proceeds as security in

connection with a loan. The resolution did not stipulate that the proceeds would be used as security in connection with a loan taken by another entity.

The resolution could also mean that the proceeds would be utilized by the bank as security in connection with a loan taken by the company itself. Thus,

from the resolution dated January 30, 2008 one cannot arrive at a conclusion that this was the first step or the starting point of a fraudulent

arrangement through which the company could facilitate the financing of the GDR subscription by Vintage. It may be noted here that when the

resolution of January 30, 2008 was passed Vintage was nowhere in the picture. The pledging of the shares on May 5, 2009 in favour of Vintage and

the loan taken by Vintage in order to subscribe to the GDR issues was done at a time when the appellant admittedly was not involved in the affairs of

the company as he had ceased to be a director prior to that date. There is no evidence to establish that the appellant Adi Cooper remained associated

with the company or with other directors even after he resigned on October 10, 2008.

9. We further find that the resolution of January 30, 2008 authorizing the bank to utilize the proceeds as security in connection with a loan cannot be

inferred as loan given to Vintage. Such presumption is farfetched and cannot hold that the appellant had intention to manipulate the market or play a fraud. Therefore, the finding of the WTM that the appellant had violated Section 12A of the SEBI Act read with Regulations 3 and 4 of the PFUTP

Regulations is misconceived and not acceptable. For facility, the said provision of Section 12A of the SEBI Act and Regulations 3 and 4 of the

PFUTP Regulations are extracted hereunder :-

â?? 12A. No person shall directly or indirectlyâ?

(a) use or employ, in connection with the issue, purchase or sale of any securities listed or proposed to be listed on a recognized stock exchange, any

manipulative or deceptive device or contrivance in contravention of the provisions of this Act or the rules or the regulations made thereunder;

(b) employ any device, scheme or artifice to defraud in connection with issue or dealing in securities which are listed or proposed to be listed on a

recognised stock exchange;

(c) engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person, in connection with the issue,

dealing in securities which are listed or proposed to be listed on a recognised stock exchange, in contravention of the provisions of this Act or the rules

or the regulations made thereunderâ??

â??3. Prohibition of certain dealings in securities No person shall directly or indirectlyâ?

(a) buy, sell or otherwise deal in securities in a fraudulent manner;

(b) use or employ, in connection with issue, purchase or sale of any security listed or proposed to be listed in a recognized stock exchange, any

manipulative or deceptive device or contrivance in contravention of the provisions of the Act or the rules or the regulations made thereunder;

(c) employ any device, scheme or artifice to defraud in connection with dealing in or issue of securities which are listed or proposed to be listed on a

recognized stock exchange;

(d) engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person in connection with any dealing

in or issue of securities which are listed or proposed to be listed on a recognized stock exchange in contravention of the provisions of the Act or the

rules and the regulations made thereunder.â??

â??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 :â?

(a) â?¦â?¦â?¦â?¦

(b) â?¦â?¦â?¦â?¦

â?¦â?¦â?¦â?¦â?¦â?¦.

(f) publishing or causing to publish or reporting or causing to report by a person dealing in securities any information which is not true or which he does

not believe to be true prior to or in the course of dealing in securities;

(k) an advertisement that is misleading or that contains information in a distorted manner and which may influence the decision of the investors;

(r) planting false or misleading news which may induce sale or purchase of securitiesâ??

10. Similarly in Adesh Jain vs Securities and Exchange Board of India (Appeal No. 217 of 2020 decided on November 19, 2020) this Tribunal held:-

â??12. Having heard the learned counsel for the parties and having given our thoughtful consideration in the matter, we are of the opinion, that the

controversy involved in the present appeal is squarely covered by a decision of this Tribunal in Adi Cooper (supra) matter. In Adi Cooper (supra) the

Tribunal interpreted the relevant words of the resolution â??to use the fund so deposited in the aforesaid bank account as security in connection with

loans if anyâ?. The Tribunal held that the loans could be taken by the Company and GDR subscription to be used as security. It was never fathomed

that the subscription amount would be used for giving loans to a third party, namely, Clifford in the instant case.

13. In addition to the aforesaid, we find that at the time when the resolution of October 19, 2007 was passed Clifford was nowhere in the picture and

therefore the concept of fraud emerging through this resolution of October 19, 2007 does not arise. There is no finding of the WTM that the appellant

was aware of this arrangement of giving a loan to Clifford was in existence or the fact that a Credit Agreement or an Account Charge Agreement

would be executed in the future. In the absence of any finding, the charge of collusion and/or fraud has not been proved. Further, by a deeming fiction, liability and/or culpability cannot be fastened upon the appellant only on the basis of a resolution dated October 29, 2007.â??

11. In Chromatic India Limited vs Securities and Exchange Board of India (Appeal No. 393 of 2020 decided on May 12, 2021) this Tribunal held:-

â??14. Having heard the learned counsel for the parties, we are of the opinion that the Resolution dated August 13, 2010 by itself does not create any

suspicion nor creates any fraudulent act. Being a signatory to the said Resolution by itself does not violate any provision of the SEBI Act or the

PFUTP Regulations.â??

12. In the light of the aforesaid, we are of the opinion that merely because the appellant was present when the resolution dated July 27, 2006 was

passed, no conclusion can be drawn that this was the starting point of the fraudulent arrangement for issuance of GDR and for opening a bank

account. The resolution does not given any indication that the appellant had knowledge beforehand that the GDR issue was the purpose to manipulate

the price or the market or that a fraud would be played upon the shareholders and the investors. We are further of the opinion that finding of the

WTM that the resolution of the Board of Directors dated June 27, 2006 provides execution of a pledge or execution of a charge agreement is wholly

erroneous, perverse and based on no evidence. The resolution also does not stipulate that the proceeds could be utilized by the bank as security in

connection with a loan taken by another entity.

13. In the light of the aforesaid, we are of the view that the appellant cannot be debarred only on the basis of being present in the resolution of the

Board of Directors dated July 27, 2006. In the absence of any evidence that the appellant had a role to play in the issuance of the GDR, the mere

presence of the appellant in the resolution of the Board of Directors dated July 27, 2006 does not make him liable for the alleged fraud that had been

committed by the Company.

14. After the judgment was reserved, the respondent have submitted a short note contending that the appellant was also chairman of the audit

committee and remuneration committee which fact is reflected in the annual report of 2009-10. We find that now new grounds are being added

without arguing the matter to buttress the findings given by the WTM. Since, Annual Reports are not part of the record before the WTM nor is there any allegation in the show cause notice to the effect that the appellant was the chairman of the audit committee. Thus, these facts which are coming

up for the first time in the short note after the conclusion of the arguments and which facts were not raised during the course of the hearing before

this Tribunal cannot be taken into consideration.

15. Even otherwise, such annual reports cannot be taken into consideration nor can it be brought on record unless it was filed as additional evidence on

an application as per the provisions of Order 41 Rule 27 of the Code of Civil Procedure which principles are applicable before the Tribunal. In the

absence of any application supported by an affidavit, such additional evidence cannot be brought on record nor can it be considered.

16. We are further of the view that in the absence of any allegation that the GDR proceeds had been diverted to the effect, the fact that the appellant

was chairman of the audit committee has no relevance. Until and unless there is evidence to prove that the appellant had a role to play in the issuance

of the GDR the additional fact is only fact is being brought on record which is wholly irrelevant to the present controversy.

17. A specific assertion was made by the respondent that the appellant was appointed as non executive non promoter independent director and that he

had a limited role to play. Evidence was given to the fact that he was not a whole time director and the appellant was paid a small remuneration for

every meeting that he attended as a non executive non promoter independent director. These facts have not been considered by the WTM for reasons

best known to the said uthority.

18. We find that the Ministry of Corporate Affairs had issued a circular dated March 25, 2011 directing that extra care should be taken in examining

cases where independent directors are identified as â??officers in defaultâ?. The circular further directs that the Registrar of Companies (RoC)

should examine whether any violation had taken place with the knowledge attributable through boards process with his consent or connivance and

whether he acted diligently or not. The Ministry of Corporate Affairs further issued a circular dated March 2, 2020 indicating that civil or criminal

proceedings should not be unnecessarily initiated against the independent directors or non executive directors unless sufficient evidence exists to the

contrary. We also find that Reserve Bank of India issued a circular dated April 23, 2015 indicating that non-whole time director should not be

considered as a defaulter unless it is conclusively established that the default had taken place with his consent or connivance.

19. Thus cogent evidence must come forward to the effect that a non executive non promoter independent director was aware of the fraud that had

been played by the Company or that he was involved in the issuance of the GDR or that GDR was being issued with his connivance. Only then such

non executive non promoter independent directors should be booked. Merely because he was part of the resolution of the Board of Directors would

not make him liable.

20. In the light of the aforesaid, the impugned order insofar as it relates to the appellant cannot be sustained and is quashed. The appeal is allowed. In

the circumstances of the case, parties shall bear their own costs.

21. The present matter was heard through video conference due to Covid-19 pandemic. At this stage it is not possible to sign a copy of this order nor

a certified copy of this order could be issued by the registry. In these circumstances, this order will be digitally signed by the Private Secretary on

behalf of the bench and all concerned parties are directed to act on the digitally signed copy of this order. Parties will act on production of a digitally

signed copy sent by fax and/or email.