BEFORE THE SECURITIES APPELLATE TRIBUNAL MUMBAI

Appeal No. 97 of 2006

Date of decision: 25.03.2008

Blue Chip Tex Industries Ltd. …… Appellant

Versus

1. Bombay Stock Exchange Ltd.
2. Securities and Exchange Board of India ..… Respondents

Mr. S.K. Sen, Sr. Advocate with Ms. Shailashri, Practicing Company Secretary for the Appellant.

Mr. P.N. Modi Advocate with Mr. Sagar Divekar for Respondent No.1.

Dr. Poornima Advani Advocate with Ms. Sejal Shah Advocate for Respondent No.2.

Coram: Justice N.K. Sodhi, Presiding Officer
Arun Bhargava, Member
Utpal Bhattacharya, Member

Per: Justice N.K. Sodhi, Presiding Officer

Whether the Bombay Stock Exchange Limited (for short, BSE) and the Securities and Exchange Board of India (for short, the Board) are justified in refusing to list 7,30,100 equity shares of the appellant company allotted on preferential basis as it failed to call from the preferential allottees the balance of Rs. 4.63 per share out of the price of Rs.14.63 determined for each share, is the short question that arises for our consideration in this appeal.

2. Blue Chip Tex Industries Ltd.-the appellant herein is a public limited company which was incorporated on 17.9.1985 and its 12,50,000 fully paid up shares of Rs.10 each are listed on the BSE. It wanted to raise further capital of about Rs.125 lacs. The shareholders of the appellant in the extraordinary general meeting held on 28.4.1995 (for short, EGM), approved the issue of equity warrants with an entitlement to equity shares to the extent of 12,50,000 equity shares on preferential basis to a select group of persons. The shareholders were informed in the EGM by the chairman of the appellant company that the value of the warrants/shares was Rs.14.63 as determined in accordance with the guidelines

dated 4.8.1994 issued by the Board on preferential issues (hereinafter called the guidelines). It is on this basis that the shareholders approved the proposal of the company and passed the special resolution to raise further capital by issue of equity warrants. At this stage it would be necessary to reproduce the relevant part of the minutes of the EGM and they read as under:

> **"……..The Chairman further informed the Members that the value of share warrants/shares is Rs.14.63, determined in accordance with the guidelines provided by SEBI,** for which a certificate of Company's Auditors, M/s. C.C. Chokshi & co. had been obtained.
>
> The Chairman thereafter proposed the following resolution as special resolution which was seconded by Mr. N.K. Khemani.
>
> "Resolved THAT pursuant to section 81(1'A), section 94(1) (a) and other applicable provisions of the Companies Act, 1956, and subject to approvals, permissions and/or sanctions of such authorities, bodies and/or persons as may be necessary and subject to such terms, conditions, alterations or modifications as may be prescribed or specified while granting such approvals, permissions and sanctions which the Board of Directors of the Company (here-in-after referred to as the 'Board') be and is hereby authorized to accept, if it thinks fit, and subject further to the right of the Board to make such modifications and alterations as it may in its absolute discretion think fit in the interest of the Company, the consent of the Members of the Company be and is hereby accorded to the Board to issue Equity Warrants with an entitlement to Equity Shares to the extent of 12,50,000 (Twelve Lac Fifty Thousand) Equity Shares to such persons whether they are Shareholders of the Company or not and at such time as the Board may in their absolute discretion think fit, inter alia, upon the following terms and conditions:
>
> (A) The basis and the terms of offer of equity warrants will be decided by the Board at the time of issue to any persons whether or not the existing equity shareholders of the company or to the employees (including Directors/workers of the company.)
> (B) The equity warrants may be issued by letter of offer or by any other appropriate manner as may be decided by the Board.
> (C) The unsubscribed equity warrants will be offered to such persons as the Board in their absolute discretion think most beneficial of the Company.
> (D) The Board be and is hereby authorized in their absolute discretion in the best interest of the company to decide about such issue of equity warrants and allotment to be made at such time or times, and in such manner including fixing the dates of conversion/allotment of equity shares as the Board think fit in accordance with SEBI Guidelines with and otherwise on such terms and conditions as may be decided and deemed appropriate by the Board.
> (E) **The price of the shares received on conversion of the warrants would be higher of the following.**

(1) The average of the weekly high and low of the closing prices of the shares during the six months before thirty days before the meeting of the share holders under section 81(1-A) of the Companies Act, 1956.

OR

(2) The average of the weekly high and low of the closing prices of the shares during 2 weeks before thirty days before the meeting of the share-holders under section 81 (1-A) of the Companies Act, 1956.

(F) The relevant date for the purpose may at the option of the Director of the Issuer Company be either one referred in **(E)(1)** above or a date thirty days prior to the date on which the holder of the warrants becomes entitled to apply for the said shares……..."
(emphasis supplied)

After the EGM, the appellant issued a letter of offer in the form of an information memorandum on 24.5.1995 to the prospective preferential buyers of equity warrants to enable them to apply for the same and that also provided that each equity warrant shall entitle the holder thereof to one ordinary share of the company of Rs.10 each at a price of Rs.14.63 per share (inclusive of premium of Rs.4.63) or at such price as would be worked out according to para 4 of the guidelines which would include such premium as may be decided by the Board of Directors when the holder of the warrant becomes entitled to apply for the said shares.

3. On 24.7.1995 the appellant company allotted to thirty applicants 7,40,500 equity warrants on preferential basis through private placement with an entitlement to equity shares on an initial payment of Rs.1.50 per warrant. These preferential allottees comprised of Directors, their relatives, the companies in which the directors were substantially interested, agents and employees of the appellant and its group companies. The Board of Directors of the appellant company in their meeting held on July 29, 1996 decided to ask the warrant holders to exercise their right to apply for equity shares at a reduced price of Rs.10 per equity share and fixed the period from 31.7.1996 upto 16.8.1996 during which the right could be exercised. This revised lower price of Rs.10 per equity share was calculated in accordance with para 5 of the guidelines by taking the relevant date as the date thirty days prior to the date on which the holder of the warrants became entitled to

apply for the said shares. As the warrant holders had already made an initial payment of Rs.1.50 per equity warrant, they were required to pay the balance of Rs.8.50 for allotment of each equity share. The warrant holders exercised their rights and 7,30,100 equity shares were allotted to them on 29.8.1996.

4. Having allotted the shares on the conversion of warrants, the appellant as per its letter dated 11.10.1996 approached BSE for the listing of those shares. The permission was not granted and BSE by its letter dated 31.10.1996 informed the appellant that the pricing of the shares was not in accordance with the guidelines. It was suggested that the appellant should approach the Board for obtaining relaxation/ no objection from it from the applicability of the guidelines. On receipt of this letter, the appellant approached the Board on 24.06.1997 seeking its no objection for the listing of the converted shares. The Board, after examining the matter informed the appellant by its letter dated 3.9.1997 that "conversion of warrants at a price of Rs.10 per share is not in accordance with SEBI preferential offer guidelines". The Board also informed the appellant that the option of selecting the "relevant date" should have been exercised at the time of the passing of the special resolution under section 81(1-A) of the Companies Act. The Board also observed in its communication that "You may, if desired, call the balance money of Rs.4.63 per share so as to make them eligible for listing." It is against this communication that the present appeal has been filed. It appears that the appellant thereafter made several representations to both BSE and the Board for granting permission to list the converted shares without calling for the balance amount of Rs.4.63 per equity share from the preferential allottees. The representations were rejected and the last letter received from the Board in this regard is dated 9.12.2005.

5. The Board realized that the practice of making preferential allotment of shares etc. at a price unrelated to the prevailing market price of such instruments was on the increase. This is obviously undesirable as the allotments are made to a select group of persons who are considered to be the promoters or persons for the time being in-charge of the affairs of the company and at the cost of the general body of shareholders. Besides, companies had also been issuing warrants to a select group of persons with a right to obtain shares in

future at a price wholly unrelated to the market. A need was felt to protect the interests of the investors who did not receive such preferential treatment by ensuring that the pricing of the preferential allotment was market related. With this object in view, the Board issued the guidelines through a press note dated 4.8.1994. Paragraphs 4, 5 and 6 of the guidelines which are relevant for our purpose are reproduced hereunder for facility of reference:

> **"4. Pricing of the issue.**- The issue of shares on a preferential basis can be made at a price not less than the higher of the following :
>
> The average of the weekly high and low of the closing prices of the related shares quoted on the stock exchange during the six months preceding the **relevant date**, or
>
> OR
>
> The average of the weekly high and low of the closing prices of the related shares quoted on a stock exchange during the two weeks preceding the **relevant date.**
>
> *Explanation :*
>
> (a) **"relevant date"** for this purpose means the date thirty days prior to the date on which the meeting of General Body of shareholders is convened in terms of section 81(1-A) of the Companies Act to consider the proposed issue; and
>
> (b) "stock exchange" shall mean any of the stock exchanges in which the shares are listed and in which the highest trading volume in respect of the shares of the company has been recorded during the preceding six months prior to the relevant date.
>
> **5. Pricing of shares arising out of warrants, etc.-** Where warrants are issued on a preferential basis with an option to apply for and get allotted shares, the issuer company shall determine the price of the resultant shares in accordance **with para 4 above.**
>
> **However, the relevant date for this purpose may, at the option of the issuer**, be either the one referred to in Explanation (a) to para 4 above or a date thirty days prior to the date on which the holder of the warrants becomes entitled to apply for the said shares." (emphasis supplied)
>
> **6. Upfront payment for warrants. –** An amount equivalent to at least 10 per cent of the price fixed in terms of para (4) above would become payable for the warrants on the date of their allotment. This amount would be adjusted against the price payable subsequently for acquiring the shares by exercising an option for the purpose. This amount would stand forfeited if the option to acquire shares is not exercised.

6. The learned senior counsel for the appellant argued that the price of the shares on conversion of warrants was required to be determined as per paragraph 4 read with paragraph 5 of the guidelines and that the "relevant date" at the option of the issuer company could either be the one mentioned in the Explanation to paragraph 4 or a date

thirty days prior to the date on which the holder of the warrants became entitled to apply for the said shares. He contended that the warrant holders became entitled to apply for the shares on 31.7.1996 and that the Board of Directors was justified to adopt thirty days prior thereto as the relevant date and on that basis the price of the share works out to less than Rs.10. According to the learned senior counsel, the price of Rs.10 per share for the preferential allotment is justified. He submitted that the guidelines did not provide that the appellant should have specified the relevant date at the time of EGM. He contends that the Board of Directors was empowered by the shareholders of the appellant company in EGM to determine the "relevant date" and that their decision in this regard was final and justified. The appellant contends that no shareholder of the company has ever made a complaint in this regard.

7. Learned counsel for BSE, on the other hand, emphasized that the objective of the guidelines was for 'protecting the interest of investors who do not receive preferential treatment by ensuring that the pricing of the preferential allotment is market related.' He took us through the minutes of EGM (reproduced above) to show that the price of preferential warrants had been determined at Rs.14.63 per share in terms of para 4 of the guidelines and that the option available to the issuer company was, thus, exercised on that day itself. In this regard, he pointed out that the shareholders had fixed thirty days prior to the date of EGM as the relevant date which was one of the options available under para 4 read with para 5 of the guidelines. He referred to para (E) of the special resolution passed in the EGM. Our attention was also drawn to the Information memorandum to support the argument that the price of the preferential equity warrant/share was determined at Rs.14.63 in the EGM and that no price below this amount could be fixed by the Board of Directors. It was pointed out that BSE was justified in not allowing the listing of the preferential equity shares because the appellant failed to collect the balance of Rs.4.63 from the preferential allottees and that it also failed to submit other details sought by BSE. The learned counsel for the Board supported the arguments advanced on behalf of BSE and argued that the Board was justified in asking the appellant that, if it so desired, it could call the balance amount of Rs.4.63 per share so as to make them eligible for listing.

8. We have heard the learned counsel for the parties. The fact that appellant company wanted to raise further capital and that it decided to issue equity warrants with each warrant entitling the holder thereof to one ordinary share of the company is not in dispute. The proceedings of the EGM have already been reproduced in the earlier part of the order and a perusal thereof leaves no room for doubt that a representation had been made to the shareholders in that meeting that the price of the equity warrants would be Rs.14.63 per warrant. It was on the basis on this price that the shareholders of the company authorized their Board of Directors to proceed with the preferential allotment of warrants to the select group of persons on private placement basis. Para 4 of the guidelines deals with the pricing of the shares issued on a preferential basis. This price is the average of the weekly high and low of the closing prices of the related shares quoted on the stock exchange either during the six months preceding the relevant date or during two weeks preceding the relevant date whichever is higher. It is, thus, clear that the price of preferential shares is fixed with reference to the "relevant date" which according to the Explanation, has to be the date thirty days prior to the date on which the meeting of the general body of shareholders is convened in terms of section 81(1-A) of the Companies Act. In the case of shares arising out of warrants, the price has to be determined in accordance with para 4 of the guidelines. However, in such a case the relevant date could be either the one referred to in the Explanation to para 4 or it could be a date thirty days prior to the date on which the holder of the warrants becomes entitled to apply for the said shares. In other words, when the price of the preferential shares is determined, the "relevant date" shall be the one referred to in the Explanation to para 4 whereas in the case of shares arising out of warrants, the issuer company shall have an option to fix the relevant date as the one referred to in the Explanation or it could be the one referred to in the second part of para 5. Since the Board of Directors is seeking authority from the shareholders to make preferential allotment, it is necessary that the shareholders are informed of the basis on which the price of the shares arising out of warrants shall be determined. It follows that the issuer company shall exercise the option of fixing the "relevant date" in the meeting of the general body of shareholders itself as that alone will give them the basis of determining the price of those

shares. The “relevant date”, in our opinion, cannot be fixed at any later point of time. If the argument of the learned senior counsel for the appellant were to be accepted that it is not the requirement of the guidelines that the relevant date should be fixed in the EGM and that it could be fixed anytime thereafter, then the shareholders would never know the basis of the price at which the preferential shares arising out of warrants shall be allotted. If the relevant date with reference to which the price of the converted shares is determined, is left open to be decided at some later time then one wonders what authority do the shareholders give to the Board of Directors for making the preferential allotment. One cannot lose sight of the fact that when preferential allotment is made under section 81 (1-A) of the Companies Act, the general body of shareholders is excluded from that allotment and that is why the law requires that the Board of Directors must obtain their sanction by way of a special resolution before such allotment is made. We cannot, therefore, countenance such a plea. The learned senior counsel referred to para 13.1.2.2 of the Securities and Exchange Board of India (Disclosure & Investor Protection) Guidelines, 2000 (which repealed the earlier guidelines prevailing at the relevant time) to contend that the subsequent guidelines contain a provision that the resolution passed in terms of section 81(1-A) must clearly specify the relevant date on the basis of which price of the resultant shares shall be calculated whereas there is no such provision in the guidelines that were prevailing at the relevant time and, therefore, it follows that at the relevant time the “relevant date” could be determined anytime after the meeting of the shareholders. This contention is also without any merit and we have no hesitation in turning it down. We have interpreted the guidelines to mean that the relevant date has to be determined in the meeting of the shareholders itself and not thereafter. The Board and the BSE also read the guidelines to mean what we have said. It appears that notwithstanding what was implicit in the guidelines, there were companies which, in the case of shares arising out of warrants, were fixing the relevant dates subsequent to the meeting of the shareholders convened in terms of section 81(1-A) of the Companies Act and, therefore, the Board while repealing the guidelines and issuing the new ones in the year 2000 and with a view to remove all doubts, made explicit what

was implicit in the earlier guidelines by adding para 13.1.2.2. This para does not say anything new and only reiterates the earlier position.

9. Again, we are unable to agree with the learned senior counsel for the appellant that the shareholders of the company had not fixed the relevant date in the EGM and had left it open for the Board of Directors to decide about the same. When we look at the minutes of the EGM and clause (E) of the resolution in particular, it becomes abundantly clear that the shareholders of the company had exercised the option to fix the "relevant date" as the date being thirty days before the meeting of the shareholders under section 81(1-A) of the Companies Act (EGM) and this is one of the options available in para 5 read with the Explanation to para 4 of the guidelines. It was on this basis, that the price of the shares arising out of warrants had to be fixed and it is not in dispute that on this basis the price works out to Rs.14.63 per share and this is precisely what the chairman at the meeting had represented to the shareholders. Having obtained the authority from the shareholders on the basis that the resultant shares would be allotted to the preferential allottees at the rate of Rs.14.63 per share, the Board of Directors is not justified to allot those shares at the reduced price of Rs.10 per share. The only justification given for the reduction in price is that the Board of Directors fixed the "relevant date" in terms of para 5 of the guidelines as the date thirty days prior to the date on which the holder of warrants became entitled to apply for the shares and that the price when worked out on this basis comes to less than Rs.10 per share. We cannot accept this justification either. We have already held that the company in the EGM had to fix the relevant date and that it did fix the same as the date being thirty days before the meeting of the shareholders under section 81(1-A) of the Companies Act and having done so, it was not open to the Board of Directors to change that date subsequently as that would alter the basis of determining the price of the converted shares. It is true that at the time of the EGM, the company had the option to fix the changed date as the relevant date but it did not do so and exercised the other option of fixing the relevant date as thirty days before the meeting of shareholders under section 81(1-A) of the Companies Act. It is on the basis of this date that the price of the resultant shares has to be worked out. Merely because the company had the option at the time of

EGM would not justify the subsequent change. This is clearly contrary to the mandate given by the shareholders in the EGM besides being contrary to the guidelines. In this view of the matter we have no hesitation in holding that the Board of Directors were not justified in allotting the resultant shares to the preferential allottees at the reduced price of Rs.10 per share and that the Board was right in observing that the company could call for the remaining amount of Rs.4.63 per share from such allottees to make the preferential shares eligible for listing. The question posed in the opening part of the order is answered in the affirmative.

In the result, the appeal fails and same is dismissed with no order as to costs.

Sd/-
Justice N.K. Sodhi
Presiding Officer

Sd/-
Arun Bhargava
Member

Sd/-
Utpal Bhattacharya
Member

25.03.2008
pw