BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No.43/2002

In the matter of:

1. Big Star Films Limited
2. Aspen Securities Pvt. Ltd.,
3. Gloxinia Financial Services Pvt. Ltd.,
4. Pratik Exim Pvt. Ltd.,
5. Khazana Finport Pvt. Ltd., Appellants

Vs.
1. Securities and Exchange Board of India Respondent No.1
2. SRG Infotec (India) Limited Respondent No.2

Appearance:

Shri Arif Bookwala
Advocate
Shri Ayaz Bilawala
Advocate for Appellants

Shri Vinay Chauhan,
Legal Officer, SEBI
Shri Amit Tandon,
Manager, SEBI for Respondent No.1

Dr. R. K. Pandey,
Representative for Respondent No.2

ORDER

The Respondent No.1 (SEBI) passed an order on 4.6.2002 holding the Appellants guilty of non compliance of the requirements of regulation 10 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (the 1997 Regulations) with reference to the acquisition of shares representing 64.38%of the share capital of SRG (Infotec) India Ltd., the Respondent No.2 herein (the Company). By the said

order the Appellants were directed to make a public announcement in terms of Chapter III of the 1997 Regulations within 45 days from the date of the order, taking 21.9.98 as the referal date for determining price of the shares, and to pay interest to the shareholders at the rate of 15% per annum on the price from 31.3.1999 till the actual date of payment of consideration to the shareholders participating in the open offer directed to be made by the said order. Claiming to be aggrieved by the said order the Appellants preferred the present appeal seeking to set aside the impugned order. They had also prayed for interim order staying the operation of the impugned order till the disposal of the appeal. After hearing the concerned parties, the prayer for interim order was allowed by the Tribunal on 16/08/2002.

The main issue in the appeal is that whether or not the acquisition of 64.38% shares of the company by the Appellants is an acquisition covered under regulation 3(1)(c) enjoying exemption from the purview of regulation 10. Regulation 3 of the 1997 Regulations exempts certain acquisitions from the purview of regulation 10, 11 and 12. Regulation 10, 11 and 12 requires the acquirer to make a public announcement to acquire shares from the other shareholders of the target company on the acquisition of shares or voting rights in a company crosssing certain limits/or acquiring control over the company, as per the Regulations. But the acquirers are not obliged to make such public announcement to acquire shares if the acquisition is one falling under the exempted categories provided under regulation 3. One of such exempted categories of acquisition is acquisition of shares pursuant to preferential allotment made by a company in pursuance of a resolution passed under section 81 (1A) of the Companies Act. Section 81 of the Companies Act provides inter alia that "Where at any time after the expiry of two years from the formation of a company or at any time after the expiry of one year from the allotment of shares in that company made for the first time after its formation, whichever is earlier, it is proposed to increase the subscribed capital of the company by allotment of further shares then (a) such further shares shall be offered to the persons who, at the date of the offer, are holders of the equity shares of the company, in proportion, as nearly as circumstances admit to the capital paid up on those shares at that date……." However, not

with standing the requirements of section 81, section 81(1A) enables the company to offer further shares to any persons whether or not those persons are holders of the company's shares on the date of offer, provided that a special resolution to that effect is passed by the company in general meeting. Regulation 3(1)(c) in the 1997 Regulations provides exemption to acquisition pursuant to preferential allotment made in terms of section 81(1A) of the Companies Act. But the exemption is not automatic. It is subject to fulfilment of the conditions provided in clause (i)and (ii) of regulation 3 (1) (c). These conditions are:

(i) Board Resolution in respect of the proposed preferential allotment is sent to all the stock exchanges on which the shares of the company are listed for being notified on the notice board;

(ii) Full disclosures of the identity of the class of the proposed allottee(s) is made, and if any of the proposed allottee (s) is to be allotted such number of shares as would increase his holding to 5% or more of the post issued capital, then in such cases the price at which the allotment is proposed, the identity of such persons, the purpose of and the reason for such allotment, consequential changes if any, in the board of directors of the company and in voting rights, the share holding pattern of the company, and whether such allotment would result in change in control over the company are all disclosed in the notice of the General Meeting called for the purpose of consideration of the preferential allotment.

There is no dispute about the number of shares acquired by the Appellants and that the acquisition crossed the threshold limit provided in regulation 10. It is also admitted that the shares were acquired pursuant to the preferential allotment made in pursuance of section 81 (1A) of the Companies Act. Compliance of the requirements of clause (ii) of regulation 3(1) (c) is also not in dispute. The fact that Appellants are persons acting in concert has also been admitted. In the report dated 29.10.99 under regulation 3(4) filed by Appellant No.5 this factual position has been admitted by the Appellants. According to the impugned order the Appellants had failed to comply with requirements of clause (i) of regulation 3(1)(c). SEBI

after citing the text of certain regulations and the factual position as per the material in its possession, has stated in para 8.4 of its order that:

> "In view of the above legal provisions and facts on record, it is clear that the acquisition of shares pursuant to a preferential allotment under section 81(1A) of the Companies Act per se, is not eligible for exemption unless the conditions stipulated in the proviso to regulation 3(1)(c) are complied with. It may be mentioned that the regulations specifically provide that exemption is available subject to the compliance of the conditions. For availing the exemption, the acquirer must comply with the stipulated conditions. In this regard, I observe from the report dated 29.10.99 that in respect of the acquisition in the instant case, the condition as laid down in clause (i) of proviso to regulation 3 (1) (c) of the said regulations has not been complied with as the copy of the Board of Resolution in respect of the preferential allotment passed on 21.09.98 was sent to the stock exchanges only on 22.9.99 i.e. subsequent to allotment of shares by way of preferential issue."

This is the only ground based on which SEBI has come to the conclusion that the Appellants had failed to fulfil the requirements of clause (i)of regulation 3(1)(c) and because of the failure to fulfil the said precondition the acquisition pursuant to preferential allotment was not considered as an exempted one.

Shri Arif Bookwala, learned Counsel appearing for the Appellants submitted that the Appellants are erstwhile partners of M/s. Silicon Valley Information Technology Corporation (Silicon Valley), that the Appellants sold the said partnership firm as going concern to the company at a consideration of Rs.240 crores, that the said consideration was discharged in the form of shares in the company issued on the basis of preferential allotment of 8 crores equity shares and 14.40 crores optionally convertible preference shares (OCPs). Learned Counsel referred to the sequence of events relating to the matter under consideration in the present appeal. He admitted that the Appellants' case was not properly handled at the time of enquiry before SEBI and as a result some information crucial to the issue could not be placed before

the enquiry officer/Chairman, SEBI, and one such crucial information was the fact of the Board resolution dated 5.10.1998 regarding the proposed preferential allotment and the evidence showing despatch of the copy of the said Board Resolution to all the concerned stock exchanges by registered post. He referred to the copy of the said resolution and the copy of letters forwarding the same to the stock exchanges and submitted that the relelvant resolution as per clause (i)regulation 3 (1) (c) required to be sent to the concerned stock exchanges is the one passed by the Board on 5.10.1998 and not the one passed on 21.9.1998. He admitted that the report filed under regulation 3(4) with SEBI vide letter dated 29.10.1999 had inadvertantly shown that the resolution passed on 21.9.1998 was forwarded to the stock exchanges on 22.9.1999 though the correct date of despatch of the resolution was 22.9.98 and in support thereof referred to letters filed along with the appeal. The Appellant had also made submissions as to intimations sent in time to the stock exchanges, in compliance of the regulation 3 (1)(c)(ii) and with reference to the Board resolution approving the allotment of shares pursuant to the approval granted by the General body of the share holders. For the purpose of determining the issue in the present appeal I do not consider it is necessary to go into the details of such post Annual General Meeting reports/communications etc.

Shri Vinay Chauhan, learned representative of the Respondent submitted that SEBI had come to the conclusion that the Appellants were not entitled to the exemption in terms of regulation 3 (1)(c) as they had failed to fulfil the pre condition of clause (i)in regulation 3 (1) (c) and that the Appellants themselves had admitted in their report filed with SEBI under regulation 3 (4) that the Board resolution passed on 21.9.98 was sent to the stock exchanges only on 22.9.99, i.e. after a delay of one year. The object of sending copy of Board resolution to the stock exchange was defeated by sending the same belatedly. He submitted that the resolution is required to be sent to the stock exchanges before allotment of shares on preferential basis takes place so as to inform shareholders/public at large the material position. By sending the said resolution after one year of passing the same and even after allotment of shares as proposed thereunder has defeated the very object of the said requirement. Shri Chauhan argued at length the scope of regulation 3(1)(c), 3 (3), 3 (4) and regulation 10 and the

reach and scope of the expression "acquirer", "persons acting in concert" etc. He had also cited few authorities in support of the legal propositions made by him. But the thrust of his argument was that the Appellants are not entitled to avail of the benefit of exemption provided under regulation 3 (1) (c) inasmuch as they had failed to fulfil the requirement of the pre condition in clause (i)of regulation 3(1)(c) having failed to send the Board resolution dated 21.9.98 to the concerned stock exchanges. He submitted that facts now brought on record by the Appellants be not taken cognizance of and the order be allowed to be sustained.

I have considered the rival contentions and the material on record. It is clear that the Respondent's conclusion that the Appellants are not entitled to have the benefit of exemption in terms of regulation 3 (1)(c) is solely based on the information furnished by the Appellants in the report filed under regulation 3(4) with SEBI. It is seen that said report was filed with SEBI vide the Appellants' letter dated 29.10.1999. In the said report under part 'c' against item I on "Date when the Board Resolution was passed for considering the preferential allotment" 21.9.98 has been shown as the relevant date. Against query at item II "When the copy of the above Board Resolution was sent to all SE's where shares of Target company are listed for being notified on the notice board" – (reg 3(1) (c)(i), the date of such notification has been stated as 22.9.1999 The Appellants' contention is that reference of the year 1999 was a typographical error. The Respondent is not ready to accept it as a clerical mistake. The declarations and reports required to be filed with the authorities are not mere formalities to be treated in a casual way. The Appellants' conduct in filing the report without taking adequate care to ensure the authenticity of the information furnished therein is blameworthy. But it appears that the Respondent has also mechanically accepted the information furnished in the report. The fact that the Appellants had wrongly furnished the year 1999 not only in the compliance date but also against item III under part 'c' of the same report against the "date when shareholders meeting was held to pass a resolution u/s.81(1A) of the Companies Act to approve the preferential allotment" The date of the share holders meeting has been shown 5th Nov 1999 (against the correct date of 5th Nov 98). It is noted that the report under regulation 3

(4) was filed with SEBI by the Appellants vide their letter dated 21.10.1999. In that context if SEBI had scrutinised the report it would have noticed that a report dated 29.10.1999 can not state that the General Meeting was held on 5..11.1999. Filing of returns and report with the authorities would not serve any purpose, unless those returns or reports are properly scrutinised and the discrepancies/mistakes are addressed. It is also seen from the report that the Appellants had forwarded to SEBI a copy of the notice of the General meeting called for on 5.11.1998 for the purpose of seeking approval by special resolution of the preferential allotment. It is noticed from the notice of the Annual General Meeting that one of the special resolutions proposed to be passed in the general body meeting scheduled to be held on 5.11.1998 was the special resolution in terms of section 81(1A) of the Companies Act, 1956 giving the consent of the company and authorising the Board of Diriectors of the company "to offer, issue, and allot 8 crore equity shares of Rs.10 each at a premium of Rs.2/- per share and 14.40 OCPS of Rs.10/- each at par for consideration other than cash to the partners of Silicon Valley Information Technology Corporation on preferential basis in one or more tranches as may be deemed appropriate on such terms and conditions and in such manner as the Board may in its absolute discretion think fit." The notices and the resolutions proposed to be placed before the General meetings of the shareholders are required to be approved by the Board of Directors of the concerned company. It is seen from the explanatory statement forming part of the notice dated 5.10.1998 of the Annual general meeting that Directors had recommended the resolution seeking approval of the consent of the shareholders in terms of section 81 (1A) of the Companies Act.

The nature of the Board resolution which is required to be sent to the concerned stock exchanges has been rightly explained by the Respondent in its order in para 8.4 in the following words –

> "The clause (i)of the proviso to regulation 3(1)(c) requires that the Board resolution in respect of the proposed preferential allotment is to be sent to the stock exchanges i.e. under clause (i)of the proviso, the resolution which is passed by the Board for

considering and placing before the shareholders at general meeting (for) the issuance and allotment of such shares is required to be notified to the stock exchanges". (emphasis supplied)

It is seen from the copy of the notice dated 16.9.1998 stated to have been sent by the company to Delhi Stock Exchange that the company had notified the exchange in terms of clause 36 of the listing agreement "that the meeting of the Board of Directors of the company will be held on 21st day of September 1998 at the registered office of the company to consider acquiring/taking over of Silicon Valley Information Technology Corporation, a Delhi based software company engaged in providing integranted business and internet solutions and its proposed modern Technology Park and Institute of Information Technology at Delhi." It is noticed from the copy of the letter dated 22.9.1998 addressed to the Delhi Stock Exchange filed along with the appeal Memorandum, that the company had informed the exchange that "the Board of Directors of the Company in its meeting held on 21st September, 1998 have duly approved the acquisition proposal of Silicon Valley Information Technology Corporation, which is engaged in providing integranted business and internet solutions and its proposed modern Technology Park and Institute of Information Technology at Delhi. The Board of Directors have further decided to appoint a reputed firm of Chartered Accountants to carry out the necessary due diligence and decide the mode of payment of consideration within a period of 3 weeks." (emphasis supplied) The Appellants have not filed in the appeal proceeding before the Tribunal, the text of the resolution stated to have been passed by the Board of directors in their meeting held on 21.9.98. However, from the communication dated 22.9.98 referred to above it is clear that there was no decision yet on the issue of shares on preferential basis for the acquisition of the business in Silicon Valley, that on 21.9.98 due diligence of Silicon Valley was yet to be completed. The decision stated to have been taken in the said Board meeting of the company, can not be said to be one "in respect of the proposed preferential allotment" referred to in clause (i)of regulation 3 (1)(c). It was only an approval for acquisition of Silicon Valley. The Appellants have filedcopy of the letter dated 5.10.1998 with the postal receipt

copy thereon, addressed to the Delhi Stock Exchange. The letter states as follows:

"Please note the Board has approved the consideration of Rs.240 crore for the acquisition of Silicon Valley Information Technology Corporation, as approved in the Board Meeting on 21.9.1998 to be paid by way of Equity shares and OCP's and the resolution passed for the same is enclosed for your record." The Appellants have also attached a copy of the said resolution, which is as follows:

> "RESOLVED THAT, in furtherance of the resolution passed in the meeting of Board of Directors, convened on 21.9.98 consideration for acquisition of running business of Silicon Valley Information Corporation be fixed for Rs.240 crores to be paid by way of preferential allotment of 800,00,000 equity shares of Rs.10 each at a premium of Rs.2/- per share and 14,40,00,000 zero per cent optionally convertible preference shares (OCPs) of Rs.10.- each at par".
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> "RESOLVED FURTHER THAT consent of shareholders be sought in the ensuing general meeting in accordance with the provisions of section 18(1A) of the Companies Act, 1956 for abovesaid preferential allotment to the partners of Silicon Valley Information Technology Corporation."

It is clear that the Board resolution dated 5.10.1998 is the resolution in respect of the proposed preferential allotment, as SEBI also rightly pointed out the resolution referred to in clause (i) of regulation 3 (1)(c) is the one passed by the Board of Directors of the company for considering and placing before the shareholders at general meeting seeking consent of the members for issuance and allotment of shares on preferential basis. In this context it is noticed that the text of the said resolution has been put in the Special Resolution forming part of the Annual General Body meeting notice dated 5.10.1998. The resolution in my view required to be sent to the concerned stock exchanges is the one passed by the Board of Directors of the company on 5.10.1998, for availing exemption under regulation 3 (1)(c).

In the appeal proceedings the Appellants have filed copies of the letters stated to have been sent by them by registered post to the concerned stock exchanges on 5.10.1998

forwardding the copy of the Board resolution dated 5.10.1998 to establish compliance of regulation 3 (1)(c) (i)on their part. This evidence is untested. The information was not available with SEBI and it had no occasion to consider the same. I do not consider that this Tribunal, should embark on an investigation to ascertain compliance of regulation 3(1) (c) by the Appellants and decide as to whether the Appellants are exempted from complying with the requirements of regulation 10. Proper agency to undertake such an enquiry in my view is SEBI. It is left to SEBI to examine the facts now brought before the Tribunal in the appeal proceedings and also if considered necessary to make further enquiries to ascertain the extent of compliance of the provisions of clause (i)of regulation 3 (1) (c) of the 1997 Regulations by the Appellants. A decision in this regard based on actual factual position is crucial for determining as to whether the acquisition is an exempted one or not. For the purpose the matter is remanded to SEBI and the impugned order is therefore set aside.

It is made clear that SEBI is at liberty to issue fresh show cause notice in the matter if so desired, and decide the matter based on the facts and in accordance with the provisions of the law. The Appellants are directed to extent full co-operation to SEBI in the enquiry. In case the Appellants fail to co-operate in the enquiry, SEBI is at liberty to pass appropriate orders based on the material available with it.

Appeal allowed by way of remand. Sd/-

C. ACHUTHAN

PRESIDING OFFICER

Mumbai,
July 25 , 2003.