BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No.58/2002

In the matter of:

Suman Motels Ltd. **Appellant**
Vs.
Securities and Exchange Board of India **Respondent**

Appearance:
Shri Burzin Somandy
Advocate

Shri Ashwini Kotian,
Advocate

Ms. Nandita Rao,
Advocate
I/b. M/s. vinod Mistry & Co., **For Appellant**

Shri J. Ranganayakulu
Jt. Legal Adviser,
SEBI

Shri Praveen Trivedi
Astt. Legal Adviser,
SEBI **For Respondent**

INTERIM ORDER

The Appellant claiming to be aggrieved by the Respondent's order dated 19.7.2002 has filed the present appeal. By the said order, the Appellant, which is operating collective investment schemes, was directed to refund the money collected by it in the schemes to the investors within one month from the date of the order. By the said order the Appellant has been informed of the consequences that would follow in case refund of money as directed is not made.

When the Appellant's prayer for interim order staying the operation of the impugned order was taken up, Shri Burzin Somandy, learned counsel appearing for the Appellant submitted that the Appellant is doing whatever it can to refund the money to the investors. He stated that the Appellant has already approached the Hon'ble Bombay High Court seeking sanction of a Scheme of Compromise / Arrangement under section 391/392 of the Companies Act, 1956 and for the purpose meeting of the creditors was called twice in the past, but could not be held because of disturbances caused by certain persons, that again the meeting has been called some time in October.

Learned counsel submitted that the impugned order has been issued without following the principles of natural justice in as much as the Appellant was not given enough opportunity of being heard and the Appellant was not favoured with certain clarifications and guidance sought by it from the Respondent, despite the Tribunal's direction in its order dated 8.9.2000 in the appeal No.11/2000 filed by the Appellant.

Learned counsel submitted that the Appellant's representative had made submissions before the Respondent's Chairman on 8.5.2002 and in the meeting the Respondent had agreed to the Appellant's schedule to repay the investors by 31.12.2002, that the Respondent is therefore estopped from asking the Appellant to make refund within a month from the date of the order. He submitted that since the Respondent having granted time to make refund by 31.12.2002, it can not insist for compliance of the

provisions of regulation 73/74 at this stage, that the Respondent is also aware of the Appellant's pending application before the Hon'ble Bombay High Court involving the issue of payment to the creditors.

Learned counsel submitted that the Respondent's order is a blanket order covering all the collective investment schemes operated by the Appellant, whereas the show cause notice which has been adjudicated was only with reference to the Appellant's Earth Bond Scheme, that the proceedings relating to other schemes are still pending and, therefore, the impugned order has gone beyond the purview of the show cause notice.

Shri Somandy, as an alternative, submitted that the Appellant should have been given an opportunity to explain its views before the order was passed, that having not done so atleast now before proceeding further in the matter the Respondent be directed to give an opportunity to the Appellant to explain its case.
Learned counsel submitted that the Appellant satisfies all the requirements justifying an interim order staying the operation of the impugned order as it has a prima facie case in its favour, that the balance of convenience is in its favour and that in case the order is enforced now the Appellant would suffer irreparable injury.

Shri Ranganayakulu,learned Representative of the Respondent submitted that the Appellant is trying all tactics to delay refund of money due to its investors. He submitted that the Respondent had never agreed to the Appellant's so called assurance to make payments by 31.12.2002 and that in any case the Respondent is not empowered to accept a proposal which is not in tune with the requirements of regulation 73 and 74.

Shri Ranganayakulu submitted that the Appellant itself had admitted the fact of receiving the show cause notice and submitted to the proceedings before the Respondent, as could be seen from the material relied on by it in the appeal, that it has filed replies and also made oral submissions before the Chairman of the Respondent on several occasions. By way of example he referred to the minutes of the meeting the Appellant's representative had with the Chairman on 8.5.2002 relied on by the Appellant itself. With reference to the allegation that the Appellant was not given clarification etc. in terms of the Tribunal's order dated 8.9.2000 in Appeal No.11/2000, Shri Ranganayakulu referred to the Appellant's letter dated 20.11.2000 addressed to the Respondent wherein it has been stated by the Appellant that "we are grateful to you for giving us guidance and co-operation from time to time". Learned Representative submitted that the Appellant is making factually incorrect submissions to misguide the Tribunal. Shri Ranganayakulu also submitted that the Appellant's petition before the Hon'ble Bombay High Court for sanction for a scheme of compromise / arrangement can not stand in the way of the Respondent directing the Appellant to make refund to the aggrieved investors as provided in the Regulations and that the Hon'ble Court has not yet passed any order approving the scheme, that the scheme is yet to have the approval of the creditors. Shri Ranganayakulu submitted that the Appellant has suppressed the fact of its filing an application before the Hon'ble Bombay High Court seeking stay of the operation of the impugned order and that the matter was argued at length and perhaps assessing that the outcome of the appeal is not likely to be in its favour, the Appellant withdrew the said application. Learned Representative submitted that investors stake in the Appellant's schemes is in danger and complaints are pouring in every day, that as of now about 600 investor grievances are pending redressal. Shri Ranganayakulu strongly urged not to grant any interim order, as the Appellant has not made out any case justifying grant of the prayer.

I have taken into consideration the submissions made on behalf of the parties in regard to the Appellant's prayer for the interim order.

The Appellant's submission that the impugned order was passed without providing opportunity of being heard is totally baseless. It is evident from the records relied on by the Appellant that the Appellant was served with show cause notice and that the Appellant had responded to the same by making written and oral submissions. It is also on record that the Appellant had received clarifications / guidelines from the Respondent in terms of the Tribunal's order dated 8.9.2000. The Apellant's contention that show cause notice under adjudication relates to the Appellant's Earth Bond Scheme and as such the order cannot go beyond the scope of the notice is also not correct, as there is not even such a suggestion in the notice that it is confined only to the said one scheme. There is absolutely no substance in the Appellant's submission that the order has been passed without complying with the rules of natural justice.

It is an admitted fact that the Appellant was operating collective investment schemes attracting the provisions of the Securities and Exchange Board of India (Collective Investment Schemes) Regulations, 1999(1999 Regulations). put in force from 15.10.1999.

Respondent is a statutory Board established under the Securities and Exchange Board of India Act,

1992 (the Act). The object of the Act is to protect the interests of investors in securities and to promote the development of, and to regulate the securities market. Section 11 of the Act enumerates the functions of the Respondent. The section mandates the Respondent to protect the interests of investors by such measures as it thinks fit. Registering and regulating collective investment schemes is one of the measures which the Respondent is empowered to take. The Respondent in exercise of the powers vested in it, has notified the 1999 Regulations, which came into force from 15.10.1999. The said Regulations in Chapter IX provide for registration of the existing collective investment schemes and also the new schemes. Existing collective investment scheme means those collective investment schemes which were operating immediately prior to the commencement of the 1999 Regulations. The Appellant was found to be operating collective investment schemes, on the date on which the 1999 Regulations came into force. It was, therefore, required to comply with the requirements set out under chapter IX of the 1999 Regulations within the stipulated time frame.

Collective investment scheme has been defined in section 11AA of the Act. Since the Appellant has admitted that it is operating collective investment schemes, no further examination about the applicability of the Regulations to the Appellant is felt necessary.

The Regulations provide for regulating the new entrant collective investment schemes and also the existing collective investment schemes. As per regulation 5 "any person who immediately prior to the commencement of the Regulations was operating a scheme, shall subject to the provision of chapter IX of the Regulations make an application to the Board for the grant of certificate within a period of 2 months from such date". Chapter IX prescribes the requirements to be followed by collective investment schemes which were operating on the date of notification of the Regulations (i.e. 15.10.1999). Since the provisions under Chapter IX have a bearing on the issues involved in the appeal, the same are extracted below:

"Existing schemes to obtain provisional registration -
68 (1) Any person who has been operating a collective investment scheme at the time of commencement of these regulations shall be deemed to be an existing collective investment scheme and shall also comply with the provisions of this Chapter.

Explanation- The expression 'operating a collective investment scheme' shall include carrying out the obligations undertaken in the various documents entered into with the investors who have subscribed to the scheme.

(2) An existing collective investment scheme shall make an application to the Board in the manner specified in regulation 5.

(3) The application made under sub-regulation (2) shall be dealt with in any of the following manner:-

(a) by grant of provisional registration by the Board under sub-regulation (1) of regulation 71;

(b) by grant of a certificate of registration by the Board under regulation 10;

(c) by rejection of the application for registration by the Board under regulation 12.

No scheme to be launched until grant of registration-
69 (1) No existing collective investment scheme shall launch any new scheme or raise money from the investors even under the existing scheme, unless a certificate of registration is granted to it by the Board under regulation10.

Consideration of application for grant of provisional registration-
70 (1)The applicant for the purpose of being considered eligible for the grant of provisional registration shall satisfy the Board that -

(a) the scheme of the applicant are in the nature of collective investment schemes;

(b) the affairs of the applicant are not being conducted in a manner detrimental to the interest of existing investors;

(c) the applicant has at least 50% independent directors at the time of making the application.

Explanation.-"Independent directors" shall mean directors who are not associates of the persons operating the existing collective investment scheme;

(d) any person, directly or indirectly connected with it has not been granted registration by the Board under the Act.

(2) The Board for the purposes of grant of provisional registration may, inter alia, inspect the schemes, books of accounts, records and documents of the applicant.

(3) The Board shall recover from the applicant such expenses including fees paid to the auditor, appraising agency as may be incurred by it for the purposes of inspecting the schemes, books of accounts, records and documents of the applicant.

(4) The Board on being satisfied that the requirements specified in sub-regulation (1) are not fulfilled may reject the applications and the applicant thereupon shall wind up its existing scheme(s) in the manner specified in regulation 73.

Grant of provisional registration-

71 (1) The Board after being satisfied that the conditions specified in regulation 70 are fulfilled may grant provisional registration to the applicant subject to the following conditions, namely:-

(a) the applicant shall get the existing schemes rated by a credit rating agency within one year from the date of grant of provisional registration.

(b) the applicant shall get the existing schemes audited by an auditor within a period of one year from the date of grant of provisional registration;

(c) the applicant shall get existing schemes appraised by an appraising agency within a period of one year from the date of grant of provisional registration;

(d) the applicant shall create a trust and appoint trustee in the manner specified in Chapter IV of these regulations within a period of one year from the date of grant of provisional registration;

(e) the applicant shall comply with accounting and valuation norms in respect of schemes floated before the commencement of these regulations as specified in Part II of the Ninth Schedule within a period of one year from the date of provisional registration;

(f) the applicant shall meet the minimum net worth of Rupees one crore within one year from the date of grant of provisional registration which shall be increased by Rupees one crore each within two years, three years, four years, and five years from the date of grant of provisional registration;

(g) the applicant shall not dispose of the scheme property except for meeting obligations arising under the offer document of the scheme;

(h) the applicant shall comply with the conditions specified in regulation 11;

(i) such other conditions which the Board may impose.

(2) The applicant shall give a written undertaking to the Board to comply with the conditions specified in sub-regulation (1).

(3) The applicant who has been considered eligible for the grant of provisional registration by the Board, shall pay provisional registration fee as per the Second Schedule.

(4) An applicant who after grant of provisional registration fails to comply with the conditions as specified in sub-regulation (1) and regulation 9 shall not be considered eligible

for the grant of certificate of registration under regulation 10 and shall wind up the scheme in the manner specified in regulation 73.

Registration to existing scheme -

72 (1) An existing collective investment scheme which satisfies the Board that the requirements specified in regulation 9 and the conditions specified under regulation 71 have been fulfilled, shall be granted a certificate of registration under regulation 10 upon payment of registration fees as specified in paragraph 2 of the Second Schedule and on such terms and conditions as may be specified by the Board.

(2) An existing collective investment scheme which has been granted certificate of registration under sub-regulation (1) may be allowed to float new schemes on such terms and conditions as may be specified by the Board.

Manner of repayment and winding up-

73 (1) An existing collective investment scheme which,-

(a) has failed to make an application for registration to the Board; or

(b) has not been granted provisional registration by the Board; or

(c) having obtained provisional registration fails to comply with the provisions of regulation 71;
shall wind up the existing scheme.

(2) The existing collective investment scheme to be wound up under sub-regulation (1) shall send an information memorandum to the investors who have subscribed to the schemes, within two months from the date of receipt of intimation from the Board, detailing the state of affairs of the scheme, the amount repayable to each investor and the manner in which such amount is determined.

(3) The information memorandum referred to in sub-regulation (2) shall be dated and signed by all the directors of the scheme.

(4) The Board may specify such other disclosures to be made in the information memorandum, as it deems fit.

(5) The information memorandum shall be sent to the investors within one week from the date of the information memorandum.

(6) The information memorandum shall explicitly state that investors desirous of continuing with the scheme shall have to give a positive consent within one month from the date of the information memorandum to continue with the scheme.

(7) The investors who give positive consent under sub-regulation (6), shall continue with the scheme at their risk and responsibility:

Provided that if the positive consent to continue with the scheme, is received from only twenty-five per cent or less of the total number of existing investors, the scheme shall be wound up.

(8) The payment to the investors, shall be made within three months of the date of the information memorandum.

(9) On completion of the winding up, the existing collective investment scheme shall file with the Board such reports, as may be specified by the Board.

Existing scheme not desirous of obtaining registration to repay-

74 (1) An existing collective investment scheme which is not desirous of obtaining provisional registration from the Board shall formulate a scheme of repayment and make such repayment to the existing investors in the manner specified in regulation 73."

On a perusal of the above cited regulations, it is clear that a collective investment scheme which was in

operation on the appointed day i.e., 15.10.1999 has three options i.e. (a) get registered with the Respondent or (b) wind up the schemes or (c) formulate a scheme of repayment and make such repayment to the investors in the manner specified in regulation 73.

In terms of regulation 65, the Respondent is empowered, in the interest of securities market and the investors, to give such directions, including directions:

> "(a) requiring the person concerned not to collect any money from investors or to launch any schemes.
>
> (b) prohibiting the person concerned from disposing of any of the properties of the scheme acquired in violation of the regulations.
>
> (c) requiring the person concerned to dispose of the assets of the scheme in a manner as may be specified in the directions.
>
> (d) requiring person concerned to refund any money or the assets to the concerned investors alongwith the requisite interest or otherwise, collected under the scheme.
>
> (e) prohibiting the person concerned from operating in the capital market or from accessing the capital market for a specific period."

The requirements to be complied with by an existing collective investment scheme are clear from the regulations cited above. The Respondent's power to issue directions is provided in regulation 65. The Respondent's order has to be viewed in the light of the requirements of the above regulations and the power of the Respondent to issue directions.

The factual position and the reason for making the order has been stated in the order itself as follows:

"SEBI vide a letter dated December 29, 1999 and also by way of a public notice dated December 10, 1999, had given intimation to the Company in terms of Regulation 73 (2) which cast an obligation on it to send an Information Memorandum to all the investors detailing the state of affairs of the scheme(s), the amount repayable to each investor and the manner in which such amount is determined. Accordingly, the Company was required to send the Information Memorandum to the investors latest by February 28, 2000.

In the meanwhile, SEBI having regard to the interest of the investors and requests received from various entities, extended the last date for submitting application for grant of registration by existing entities upto March 31, 2000. The same was intimated by SEBI to the Company vide a letter, a press release and a public notice. However, the company still did not apply for grant of registration with SEBI in terms of the said regulations.

As a matter of fact, the Company, neither applied for registration under the said Regulations nor has taken any steps for winding up of the scheme(s) and making payment to the investors in the manner provided under the said Regulations and has prima facie violated the provisions of Section 12 (1B) of SEBI Act, 1992 and Regulations 5(1) read with Regulation 68(1), 68(2), 73 & 74 of the SEBI (Collective Investment Schemes) Regulations, 1999.

SEBI had also issued a public notice in various newspapers in this regard inviting attention of the concerned entities including the Company herein about the statutory requirements under the provisions of SEBI Act and the said Regulations.

Further, by way of a Show Cause Notice dated May 12, 2000, the Company was asked to show cause as to why the action mentioned therein be not initiated against it for the aforesaid violations / non-compliance. The Company vide its reply dated May 16, 2000 informed SEBI that Information Memorandum has been circulated to its members on 28-02-2000 and it has taken further steps for realizing the assets and for making payments to the investors. Further, the Company vide its letter dated October 4, 2000 submitted that it will be submitting the "Winding Up and Repayment Report" to SEBI in a short while. However, the Company has failed to wind up its Collective Investment Scheme(s) to make repayments to its investors and submit the "Winding Up and Repayment Report" to SEBI in accordance with the said Regulations, despite its confirmation to do so.

As requested the Company was granted personal hearings on February 6,2001, February 7, 2001 February 20, 2001 June 20, 2001, September 26, 2001 December 4, 2001, February 11, 2002 and on May

08, 2002 before Chairman, SEBI to explain the reason of such non compliance of the said Regulations. The said hearings were attended by the Company officials wherein they submitted that the Company does not want to continue with its Collective Investment Scheme(s) and therefore it has not applied for registration. However, they promised that the Company is taking all the steps for the repayment to the investors and sought further time for such repayment to the investors.

During the personal hearing on 26.09.2001, which was attended by Shri Mukhtar Hussain, Chairman and Shri Surnedra Khandhar, Managing Director of te Company, both of them had given a written assurance to SEBI, interalia, to the effect that the Company would make all the efforts to repay the investors at the earliest but not later than December 31, 2002, it would make an application in Company Application No. 340/2001 filed by it before the Hon'ble Bombay High Court amending the proposed scheme of repayment in terms of the aforesaid assurance and shall also publish this commitment in four newspapers within 45 days from the date of such commitment. During the hearing it was noted that the Company has made contradictory statements regarding the number of its Collective Investment Scheme(s), number of investors therein and amounts raised under its Collective Investment Scheme(s).

When the enquiry was made during the personal hearing on 08.05.2002 regarding the compliance of the aforesaid commitment, the officials of the Company could not offer any evidence to establish that they have complied with any of such commitment.

Therefore, having regard to submissions made by the Managing director of the Company during the said hearing and after taking into consideration the interest of investors, the Company was directed, interalia:

1. to take immediate steps to redress the investors complaints;
2. to take steps to fulfil its commitments dated September 26,2001, and
3. to submit a detailed compliance report with SEBI by May 20, 2002.

While the Company forwarded letter dated May 18, 2002 and July 8, 2002 submitting certain information, it has failed to comply with the aforesaid directions and file the compliance report in terms of directions given during personal hearings dtd. 08.05.2002.

Proceedings have been held on number of occasions. Opportunity has been given on several times. Having regard to the above, I am of the view that the Company has been given number of opportunities for making repayment to the investors. At every occasion, the representative of the company has assured SEBI that it would repay the investors and would take every possible action in this regard. However, the conduct of the company is such that it wants to pay lip service to what is committed to SEBI. Therefore, I am constrained to take a view, on the basis of the facts of the case, that the Company is not serious about fulfilling its promises and making the repayment to the investors. In any case, the fact remains at the Company, has not complied with SEBI (CIS) Regulations, 1999."

In the said context the Respondent passed the following order:

"In exercise of the power conferred upon me under section 11B of the SEBI Act, 1992 read with Regulation 65 of SEBI (CIS) regulations, I hereby direct the Company to refund the money collected under its Collective Investment Scheme(s) with returns which is due to the investors as per the terms of the offer within a period of one month from the date of this Order failing which the following actions would follow:

Initiation of prosecution under section 24 of SEBI Act, 1992 which prescribed imprisonment for a term which may extend to one year, or with fine, or with both against the Company /its promoters/ its directors/managers/ persons in charge of the business of its scheme (s).

The company/ its promoters/ directors/ managers/ persons in charge of the business of its scheme(s) would be debarred from operating in the capital market and from accessing the capital market for a period of 5 years.

Writing to the state government/ local police to register civil/criminal cases against the Company/its promoters/ directors/managers/persons in charge of the business of its scheme(s) for the offences of fraud, cheating, criminal breach of trust, dishonest misappropriation of public funds.

Writing to the Department of Company affairs to initiate the process of winding up of the Company."

On a perusal of the material on record it is evident that the Appellant has not complied with the requirements of regulation 73 and 74 even though it is almost 3 years by now the Regulations are in operation. The Respondent's direction is to refund the money in terms of the regulations. The Appellant's argument that the Respondent had agreed to its proposal to make refund by 31.12.2002 mainly relying on the minutes of the meeting the Appellant's representative had with the Chairman of the Respondent on 8.5.2002, can not be taken in isolation. There were other requirements as well to be complied with. But there is no indication of compliance of those requirements. In this context it would be useful to have a look at the text of the directions stated to have been given by the Chairman, as recorded in the minutes of the said meeting. What the Chairman had directed, as per the minutes are as under:

> "Having regard to the above and after taking into consideration the interests of the investors, Chairman, SEBI directed as under:
>
> i) SML to immediately submit (but not later than May 20, 2002) to SEBI a copy of its registers of repayment claimed to have been made by it to its CIS investors.
>
> ii) SML to take immediate steps to fulfil its aforesaid commitments. A detailed report on the steps taken along with the information/documents not submitted so far by it to SEBI to be filed by SML with SEBI on or before May 20, 2002.
>
> iii) SML to submit to SEBI by May 20, 2002 a certificate from its statutory auditors regarding scheme wise repayment claimed to have been made by it to its investors of CIS.
>
> iv) SML to discuss with IGF the suggestions made by IGF regarding early repayment to be made to its investors, modify its proposal (pertaining to the scheme of compromise filed by it earlier before the Hon'ble Court) after incorporating the said suggestions, move the Hon'ble High Court of Mumbai for the modification of the scheme of compromise and submit a copy of the modified scheme to SEBI by May 20, 2002.
>
> v) SML to redress the grievances of investors which were forwarded by SEBI to it as well as of those investors who were present in the hearing and to submit a report to SEBI in this regard by May 20, 2002.
>
> vi) SEBI to give a copy of the minutes of the personal hearing to SML."

Shri Somandy's argument that the Respondent is estopped from directing the Appellant to make payment to investors within a month is not acceptable as there is no estoppel against law. The direction is to refund the amount due to the investors as per regulation 73/74 as the Appellant has not got itself registered under regulation 72. Learned counsel had submitted that the order is not for complying with the requirements of the Regulations but on the failure to comply with the commitments made by the appellant. This submission in my view is without realising that these commitments are relatable to compliance of the Regulations and not something outside the purview of the Regulations.

It is to be noted that the Respondent has not passed any order under the Act debarring the Appellant, as stated at item (2) of the order. Initiating action to launch criminal prosecution or writing to the authorities requesting to take appropriate action by them by itself is not a matter against which an appeal lies to the Tribunal. The Tribunal can not stop the Respondent taking the steps referred to in the order. In case the Respondent passes an order debarring the Appellant / directors / officers etc. from accessing /operating in the capital market etc., referred to at item (2) of the order, such a direction is appealable and the appeal, if filed, will be decided on merits. The fact that the Appellant has moved the Hon'ble Bombay High Court under the provisions of the Companies Act seeking sanction for a scheme of compromise or arrangement by itself does not take away the Respondent's power under the Act or the Regulations made thereunder to take investor protection measures. The Hon'ble High Court has not passed any order approving the scheme under contemplation.

The Appellant has failed to make out a prima facie case in its favour. The Appellant has not established that the balance of convenience is in its favour or that if the order is not stayed temporarily it would cause irreparable injury to the Appellant. In the light of the facts and circumstances of the case as put forth before me, I do not find any justification to interfere with the order at this stage. Therefore, the Appellant's prayer for interim order staying the operation of the impugned order is not allowed.

The Registry, on receipt of the reply from the Respondent will list early the appeal for disposal.

Sd/-

(C.ACHUTHAN)
PRESIDING OFFICER

Place: Mumbai
Date: September 19, 2002