BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

APPEAL NO 12/2000

In the matter of

VLS Finance Ltd. **Appellant**

Vs.

Shri P. Sri Sai Ram
Adjudicating Officer
Securities & Exchange Board of India **Respondent No. 1**

Track Parts of India Ltd. **Respondent No. 2**

APPEARANCE

Mr. Mahendra Bhuta
Company Secretary
Mahendra Bhuta & Associates

Mr. Alkesh Goradia
Representative of the Appellant **for Appellant**

Mr. Ananta Barua
Division Chief, SEBI **for Respondent No. 1**

Mr. Adesh Tandon
Company Secretary
Adesh Tandon & Associates **for Respondent No. 2**

ORDER

This appeal by VLS Finance Ltd., the Appellant herein, is against the order dated 20.4.2000 made by the Adjudicating Officer, imposing a penalty of Rs.5 lakhs under section 15H(i) of the Securities and Exchange Board of India Act, 1992 (the Act), based on the finding of an inquiry made by him that regulation 6 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1994 (the regulations) has been violated by the Appellant.

Background of the appeal emerging from the impugned order is as follows:

The Appellant is a public limited company incorporated under the Companies Act, 1956. It is a listing Non-Banking Finance company, interalia, engaged mainly in the business of lease financing, hire purchase, financing and financial consultancy. Respondent No.2 (the Respondent Company) is also a public limited company incorporated under the Companies Act engaged in the manufacturing business. The Appellant had advanced a loan of Rs.2 crores (subsequently raised to Rs.2.40 crores) to the Respondent company, in pursuance of an

agreement dated 18.2.1995 entered into between them. By the said agreement the Respondent Company under took to secure the said loan by way of demand promissory note which was to be a continuing security to the Appellant for the monies which may become due from the Respondent Company. To secure the loan facility the promoters and their family members and associate members of the Respondent Company agreed to pledge some of their shares by way of collateral security with the Appellant. In terms of the said agreement some of the promoters, directors and family members and group companies of the Respondent company executed in favour of the Appellant respective Deed of Pledge dated 18.2.1995 whereby they deposited and pledged with the Appellant the shares of the Respondent company owned by them, together with blank transfer form intended as creditors security for repayment of the loan amount alongwith interest accrued thereon. The Respondent Company and the various pledgers breached the terms and conditions of Deed of Pledge, by failure to pledge additional shares by way of security as covenanted and undertaken in the said agreement. Out of the shares so pledged, 51, 500 shares belonged to one Sameer Bhargava and others of the promoter group. With the shares pledged, the promoters had provided blank transfer forms and as per the agreement, promoters were to provide fresh transfer forms upon expiry of any of the transfer forms for shares pledged, till the repayment of the loan amount with interest accrued thereon in full. However, the holders of the said 51,500 shares refused to their commitment and also refused to provide fresh transfer forms and instead demanded return of the shares pledged by them. In this context, to protect its interest, the Appellant got the shares transferred in its name on 27.11.1995. However, these shares were re-transferred to the original holders on 30.5.1996 in terms of settlement reached as between the parties in a petition filed before Company Law Board by the share owners. However, the Securities and Exchange Board of India (SEBI) took up the matter for inquiry on a complaint received by it alleging violation of the take over regulations by the Appellant and appointed by Adjudicating Officer to inquire into the alleged contravention of regulation 6 of the 1994 Regulations and impose penalty in case so warranted, as provided under section 15H of the Act. The Adjudicating Officer, after inquiry came to the conclusion that the Appellant was guilty of violating regulation 6 and imposed a sum of Rs.5 lakhs as penalty, as provided under section 15H(i) of the Act.

Shri Mahendra Bhuta, learned Representative of the Appellant submitted that the Appellant had not acquired any shares of the Respondent company in contravention to the provisions of regulation 6 to warrant penalisation under section 15H of the Act. He submitted that the Appellant being a finance company, during the course of its business had advanced loans to the Respondent company on mutually agreed terms and conditions and one of such conditions was to provide collateral security of shares of the Respondent company owned by its promoters, directors and their relatives and group companies. It was an accepted condition that the pledgers alongwith the share certificates will furnish blank transfer forms to enable the Appellant to transfer the shares so pledged in its name to protect its interest. Accordingly, blank transfer forms were given to the Appellant along with share certificates. The holders of 51,500 shares did not agree to furnish fresh transfer forms in place of the forms provided by them, the validity of which were to expire due to efflux of time and they were demanding return of the share certificates, though the loan amount was still due from the Respondent company. In that context, the Appellant was left with no choice but to get the shares transferred in its name to protect its interest otherwise the very purpose of pledging the shares would have become redundant. He submitted that the Appellant is also a limited company with obligations to protect the financial interests of its share holders. He pointed out that 51,500 shares were transferred in its name on 27.11.1995 and the moment the holders of those shares agreed to furnish blank transfer forms, a mutual settlement was arrived at, the same was endorsed by Company LAW Board, in a petition filed by the owners of the said shares, the hares were re-transferred to the original owners on 30.6.1996, though these shares continued to be part of the collateral security against the loan amount given to the Respondent company. Shri Barua submitted that it was never the intention of the Appellant to acquire shares and that it had no plan to manage or control the affairs of the company so as to attract the provisions of the 1994 Regulations. The transfer of shares, which the Adjudicating Officer identified as trigger point attracting the provisions of the Regulations, was actually exercise of a remedial measure pre-determined by the parties through an agreement. If the Appellant had not taken such measure, the pledged shares would not have been of any security, as the right to dispose of those shares

would have gone back to the owners, after the validity of the transfer forms expired. He submitted that the Appellant is being targeted to harass in the wake of the ongoing group rivalry among the promoters of the Respondent Company. He submitted that group rivalry had virtually brought the business activities of the Respondent Company to stand still.

Shri Bhuta cited the observations made by the Adjudicating Officer in para 6.8 of the impugned order as endorsing the Appellant's view point that the shares were transferred by the owners of those 51,500 shares to the appellant, by way of pledge to secure the loan given by the Appellant to the Respondent company and the Appellant did not own these shares. Shri Bhuta submitted that the Adjudicating Officer having admitted that the Appellant was not the owner of the shares erred in concluding that the transaction attracted regulation 6. He submitted that the finding of the Adjudicating Officer that the act of getting the equity shares transferred in its name, in the context of refusal by the pledgers of the respective shares to provide fresh transfer forms is acquisition of shares, in terms of the regulation is not legally tenable. He has contended that any transaction which does not result in change in ownership is not an acquisition. In support of this version he cited Supreme Court's observation in Devidas Gopal Krishnan Vs. State of Punjab (AIR 1967 SC 1895) that "Acquisition is the act by which a person acquires property in a thing. `Acquire' is to become the owner of the property. One can, therefore, acquire a property either by voluntary or involuntary transfer". He submitted that in the light of the said view of the Supreme Court, ownership is an essential and integral part of any act or activity to be termed as acquisition. According to the learned Representative the expression "owner", unless a statute in its definition connotes otherwise, means availability of all rights attached to property on permanent basis till the ownership continues without interference from other and to the exclusion of others. He submitted that in the instant case, the beneficial owners of the shares were persons other than the Appellant and the rights of the Appellant as per agreement were not unfettered. The Appellant, therefore, cannot be treated as absolute owner of the shares in question. He also cited respondent SEBI's version in the case of acquisition of shares of ACC Cements Ltd. by Gujarat Ambuja Cements Ltd. that "Acquisition of the share did not mean a change in the control unless the buyer had the majority on the Board of Directors". In this context the learned Representative submitted that the Appellant had got transferred just 7.36% of the capital in its name, as an ad-hoc measure, without any object of effecting any change in the structure of the Board of Directors or for exercising any type of control over the Respondent company. In the Adjudicating Officer's own version the Appellant was not the owner of the shares in question. But still he held the Appellant guilty of non-compliance of regulation 6 of the 1994 Regulations. Referring to the several course of actions available to the Appellant as raised by the Respondents, the learned Representative submitted that it was for the Appellant to decide as to which course was to be adopted in its interest. He submitted that vide letter dated 10.3.1995 placed at Annexure 1 to the appeal, the Appellant had served notice on the Respondent company stating its decision to transfer the shares in its name in case the said Respondent fails to comply with the undertaking given in the agreement. According to him the allegation that the pledge property was acquired without notice was baseless. He denied the charge that the transaction in question was acquisition in terms of 1994 Regulations.

Shri Ananta Barua, appearing for the Respondent SEBI, submitted that admittedly the Appellant had acquired 51, 500 shares constituting 7.36% of the paid up capital of the Respondent company, whereby attracting the provisions of the 1994 Regulations and 1997 Regulations. Since the Appellant became the registered holder of 51, 500 shares of the Respondent Company, it became the legal holder of the said shares. He referred to the definition of the expression "acquirer" provided under regulation 2(b) of the 1994 Regulations and submitted that as per the said definition, the Appellant is an acquirer. He further pointed out that for attracting the provisions of regulation 6 of the 1994 Regulations and submitted that as per the said definition, the Appellant is an acquirer. He further pointed out that for attracting the provisions of regulation 6 of the 1994 Regulations, it was not necessary that the person should own the shares or control the affairs of the Target Company. Any acquirer holding shares as acquired in the manner prescribed in the regulations would be covered for the purpose of the regulation. He further submitted that the regulation does not exclude from its ambit the

acquisition of shares by effecting transfer of the pledged shares owned by the defaulters. In fact wherever exemption was considered necessary, the Regulations have provided the same explicitly. Acquisition of the shares in the instant case is not an exempted acquisition. He submitted that intention to not to interfere in the management of the Respondent company or to acquire control over it does not absolve the Appellant from the statutory obligation of complying with the provisions of regulation 6. He further submitted that the view taken by the Respondent in the case of acquisition of shares of ACC Cements ltd. by Gujarat Ambuja Cements cannot be applied to the instant case as it was a matter covered under 1997 Regulations and not under 1994 Regulations.

Mr. Barua submitted that if a view is taken that shares acquired by way of transfer of pledged shares are not covered under the Regulations, the very object of making the Regulations will be negated as interested persons will first create an artificial pledge and thereafter get the shares transferred in their name and through this route company's management / control will be acquired with impunity. He further submitted that the very transfer of shares by the Appellant in its name was wrong, even if it is assumed that the pledgers had defaulted as the transfer was done without giving proper notice to the parties as required under law.

According to Shar Barua in terms of regulation 6(1) an acquirer who holds 5% or less than 5% shares in a company, and acquires more than 5% shares, unless covered under the specific exemption provisions of the 1994 Regulations, is required to disclose the aggregate of his holding therein to the company and also to all the stock exchanges where the shares are listed within the time frame as stipulated in the regulation. He submitted that transfer of the pledged shares without following the statutory requirement was not the only remedy available to the Appellant to protect its interests. The Appellant was at liberty to initiate civil proceedings or to seek specific performance of the concerned agreement. The submission of the Appellant that the promoter groups were fighting and the Respondent company had become non-functional because of such group fighting, etc. are not of any consequence as far as the conduct of the Appellant is concerned with reference to the compliance of the provisions of regulation 6.

The Respondent Company was represented by Mr. Adesh Tandon in the hearing. The learned Representative endorsed the submission made by the Respondent SEBI and submitted that the cope of regulation 6(1) was wide enough to cover the instant transaction as sub-clause (c) of section 6(1) refers to acquisition in any other manner not covered by sub-clause (a) and (b) of the regulation. He submitted that the fact that the Appellant acquired 51, 500 shares constituting 7.36% of the equity capital of the company on 27.11.1995 remains admitted. It is on record that the Appellant had failed to report the said acquisition to the Respondent Company and the concerned stock exchanges within the stipulated time. It is also an undisputed fact that with the registration of the shares held by the Appellant in the Respondent Company's register, the Appellant became its member. It was of no great significance as to in what circumstances the Appellant acquired shares and for what purpose it was transferred. The fact is that the Appellant acquired shares beyond the limit prescribed by regulation 6 warranting compliance of the requirements of the regulation but did not do so and thereby attracted the penal consequences.

Learned Representative submitted that the Takeover Regulations are statutory regulations. Private contract cannot over ride the substantive provisions of the law. The contention that the interse agreement enabled the Appellant to transfer the ownership of those shares does not mean that the transfer is immune from the requirements provided under the law. He submitted that ownership of the shares is not the deciding factor as contended by the Appellant, the right to vote is important. The Appellant acquired the voting right by getting its name entered on the Respondent Company's register of members on 27.11.1995. He pointed out that the Appellant was not short of other remedies to safeguard its interest and it could have protected its interest by pursuing one of those remedies, without resorting to a measure ignoring the attendant legal requirements.

Since the Appellant had relied on an order of Company Law Board, based on which the shares in question were re-transferred to the original holders and the copy of the order was not readily available at the time of hearing, the Appellant was directed to file a copy of the same in the Tribunal within 15 days from the date of hearing and simultaneously forward a copy to the Respondents. The Respondents were asked to file their submission thereon within 7 days of receipt of the order copy from the Appellant. It is seen that even though the Appellant filed a copy of the relevant order on 26th September 2000 stating that copy of the order has been served on the respondents, they did not file any reply / material in this regard. I have perused the said order. It is seen that Company Law Board Order is nothing but an endorsement of the mutual settlement arrived at by the Appellant and the parties, paving way for re-transfer of the shares to the original holders.

It is considered necessary to have a close look at the substantive portion of the impugned order at this juncture. In para 6.9 of the order, the Adjudicating Officer has summarised his findings as under:

> "I find that VLS is a Merchant Banker, VLS is not like an ordinary person, who may not have knowledge of SEBI Regulations. As a Merchant Banker, they should be particular about compliance of SEBI Regulations. There is no specific provision in the SEBI (Substantial Acquisition of Shares & Takeovers) Regulations, 1994 to indicate exemption in respect of acquisition of shares for securing a loan transaction through pledge of shares. The transaction in this case related to acquisition of shares of more than 5% of the paid up capital of TPIL. Those shares stood transferred in the name of VLS on 27.11.1995. That means the name of VLS appeared in the Register of shareholders of the company w.e.f. 27.11.95. VLS was required to disclose the aggregate of the shareholdings to the Stock Exchanges of Delhi and Kanpur where the shares of the Company were listed. That was required to be done within 4 days from the date of the acquisition as per Regulation 6(1) and 6(2) of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1994. Normally, the acquirer was required to make such disclosure within 4 days from the date of acquisition of shares i.e. the date of the agreement (signing of Transfer form). In this case, the acquirer should have at least made such disclosure within 4 days from 27.11.95, the date of transfer in their favour in the books of the company. VLS did not do that. As such, VLS violated Reg (6) ibid and consequently, Section 15(H)(i) of the Securities and Exchange Board of India Act, 1992. Section 15(H)(i) provides that a person who violates that provision shall be liable to a penalty not exceeding Rs.5 lacs."

In para 7.1 of the order he has stated that:

> "In view of what is stated above, I find that penalty can be levied in these legal proceedings in respect of violation of Regulation 6 of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1994. In para 6.9 above, I held that VLS Finance Ltd. the acquirer violated Regulation 6 ibid and consequently violated Section 15(H)(i) of the Securities and Exchange Board of India Act, 1992. Therefore, in terms of Section 15H(i) of the Securities and Exchange Board of India Act, 1992 a penalty of Rs.5, 00,000/- (Rupees Five lacs) is imposed on VLS Finance Ltd."

It is seen from the portions of the impugned order extracted above that Adjudicating Officer had come to the conclusion, in the light of the admitted fact that 51,500 shares, which exceeded 5% of the paid up capital of the Respondent company, stood transferred in the name of the

Appellant on 27.11.1995. Consequentially, the Appellant, in terms of regulation 6 was required to disclose within four days from the date of acquisition,, its aggregate share holdings in the Respondent company to the stock exchanges at Delhi and Kanpur where the shares were listed. Since the said requirement was not complied with, penalty of Rs.5 lakhs provided under section 15H(i) was imposed.

The charge that the Appellant became the holders of 51, 500 shares of the Respondent company, which constituted 7.36% of its paid up capital stands proved in the light of the Appellant's own submission. The said acquisition exceeded the statutory limit and warranted reporting as required under regulation 6 of the 1994 Regulations also stands established. However, it is felt that the decision of the Adjudicating Officer, imposing Rs.5 lakhs as penalty invoking the provisions of section 15H need detailed examination. In this context, it is considered necessary to have a close look at the provisions of regulation 6 of the 1994 Regulations and section 15H of the Act. Regulation 6 is as under:

"Acquisition of 5% and more shares of a company:-

6 (1) Any acquirer, who holds five percent or less than five per cent shares in a company and acquires more than five per cent shares:-

(a) in pursuance of a public issue; or

(b) by one or more transactions; or

(c) in any other manner not covered by (a) and (b) above,

shall disclose the aggregate of his shareholding in that company to the company and to all the stock exchanges where the shares are listed.

(2) The disclosures mentioned in sub-regulation (1) shall be made within four working days of: -

(i) the receipt of intimation of allotment of shares in respect of shares acquired under clause (a) of sub-regulation (1) or;

(ii) the acquisition of shares, as the case may be.

(3) Every company, whose shares are acquired as referred to in sub-regulation (1) shall disclose to all the stock exchanges, where the shares are listed the aggregate shareholdings of that company of all such persons within seven days of receipt of information under sub-regulation (1)."

Section 15H of the Act is as under:

"Penalty for non-disclosure of acquisition of shares and takeovers.

15H. If any person who is required under this Act or any rules or regulations made thereunder, fails to:-

(i) disclose the aggregate of his shareholding in the body corporate before he acquires any shares of that body corporate; or

(ii) make a public announcement to acquire shares at a minimum price, he shall be

liable to a penalty not exceeding five lakh rupees".

It is seen from the statutory provisions extracted above that in terms of regulation 6, acquisition of five percent or more shares of a company is required to be disclosed to the company and the concerned stock exchanges, by the acquirer within four days of the acquisition of the shares, and certainly not before the acquisition. Section 15H(i) which the Adjudicating Officer had invoked to penalise the Appellant for the violation of regulation 6 is not applicable to the instant case of default as section 15H(i) is applicable only in the case of failure to disclose the aggregate of the acquirer's share holdings in the target company before he acquires any shares of that company. It is clear that the disclosure requirement provided under regulation 6 is a post acquisition requirement whereas the penalty provided under section 15(i) is for failure to comply with the requirement whereas the penalty provided under section 15(i) is for failure to comply with the pre acquisition requirement. So section 15H(i) cannot be invoked to penalise the Appellant, who according to the Adjudicating Officer had failed to comply with the requirements of regulation 6.

It is well settled that mere mention of a wrong provision of law, when the power exercised is available even though under a different provision is by itself not sufficient to invalidate the exercise of that power. There is a plethora of Supreme Court decisions of this dictum. Keeping in mind the said principle I have perused the provisions of the Act, to find out whether there is any other provision in the Act, under which monetary penalty as levied by the Adjudicating Officer is leviable for default under regulation 6. In my effort, I stumbled on the provisions of section 15A(b) of the Act. Under the said section if any person who is required under the Act or any rules or regulations made thereunder "to file any return or furnish any information, books or documents within the time specified therefor in the regulations, fails to file return or furnish the same, he shall be liable to a penalty not exceeding five thousand rupees for every day during which such failure continues". As far as the default part is concerned, i.e. failure to report the aggregate share holding of the acquirers, to the stock exchange and the company, the same squarely fits into the ambit of the said section 15A(b). Even though this section does not refer to the requirement to `disclose', on a realistic interpretation it can be concluded that the, failure to disclose the holdings to the company and the concerned stock exchange within the stipulated time by an acquirer would come under the purview of the section.

Now comes the question as to whether the penalty levied / leviable under section 15H can be considered as the penalty levied / leviable for the default identified under section 15A(b). It is seen that section 15H provides for a penalty for exceeding Rs.5 lakhs where as section 15A(b) provided for a penalty not exceeding five thousand rupees for every day during which such failure continues. It appears that the wording of these sections that the default under section 15H(i) is a one time default where as the default under section 15A(b) is a continuing default and penal provision has designed separate penalty to meet with the defaults under these 2 sections taking into consideration the nature of the defaults. In any case, in terms of section 15J of the Act while adjudicating quantum of monetary penalty, the Adjudicating Officer is required to have due regard to the following factors, namely: -

(a) the amount of disproportionate gain or unfair advantage whenever quantifiable, made as a result of the default;

(b) the amount of loss caused to an investor or group of investors as a result of the default;

(c) the repetitive nature of the default.

It is seen from the impugned order that the Adjudicating Officer had gone to the extent of imposing the maximum penalty of Rs.5 lakhs on the Appellant in this case. There is no indicating in the order as to whether any one or all of the factors provided under section 15J guided the Adjudicating Officer to decide the maximum penalty. Since the Adjudicating Officer had opted to go for the maximum penalty, it was incumbent on his part to refer to the

specific factors provided under section 15J which guided him to impose the maximum penalty.

Since it is not clear as to what weighed in the mind of the Adjudicating Officer and which factor in section 15J persuaded him to impose the maximum penalty, it is not possible for this Tribunal to substitute the said penalty of Rs.5 lakhs as penalty under section 15A(b) of the Act. In this context it is also seen from sub-section (a) of the same section 15A that for similar default involving failure to report certain matters to SEBI, the maximum penalty leviable is only Rs.1.50 lakhs. It is for the Adjudicating Officer to dispassionately decide as to whether any monetary penalty is justified in the facts and circumstances of the case, and if the imposition of penalty is justified to decide the quantum of penalty taking into consideration of factors provided under section 15J with reference to default under regulation 6, made out in the order. For the purpose, the matter need be remanded to the Adjudicating Officer and consequently the impugned order need to be set aside. I do so accordingly. It is made clear that the Adjudicating Officer, will decide the penalty, if considered necessary, taking into consideration all the relevant aspects and legal provisions including the views expressed by the Supreme Court in Hindustan Steel Ltd. Vs. State of Orissa (AIR 1970 SC 253) and also after giving the Appellant a reasonable opportunity to putforth its point of view.

For the reasons stated above, the appeal is allowed by way of remand.

(C. ACHUTHAN)
PRESIDING OFFICER

Place: Mumbai
Date: 31.10.2000