

**BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA  
CORAM: RAJEEV KUMAR AGARWAL, WHOLE TIME MEMBER**

**ORDER**

**UNDER SECTIONS 11(1), 11(4) and 11B OF SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 AND SECTION 12A OF THE SECURITIES CONTRACTS (REGULATION) ACT, 1956- IN RESPECT OF ZENITH INFOTECH LTD.**

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1. Zenith Infotech Limited ('ZIL/company') is a public limited company having its shares listed on the Bombay Stock Exchange Ltd. ('BSE') and the National Stock Exchange Ltd. ('NSE'). The Integrated Market Surveillance System (IMSS) of the Securities and Exchange Board of India ('SEBI'), generated an alert on the sudden change in the price of the scrip of ZIL. Meanwhile, the SEBI also received complaints against ZIL *inter-alia* alleging the following:
  - i. The affairs of the company are carried out in a manner which could be catastrophic for the retail investors and shareholders of the company.*
  - ii. The promoters of the company willfully omitted to disclose, certain key transactions, information about company's financial standing and material price sensitive information to the stock exchanges.*
  - iii. The company defaulted on its obligation to redeem the FCCBs due in 2011 resulting in loss of shareholder value.*
2. The matter was, therefore, taken up for preliminary inquiry which revealed that Mr. Rajumar Saraf, Mr. Akash Kumar Saraf, Ms. Devita Saraf, Ms. Vijayrani Saraf, VU Technologies Private limited and Zenith Technologies Private Limited are all promoters of ZIL and they together hold 64.89% of its shareholding (as on December 31, 2012). Mr. Rajkumar Saraf and Mr. Akash Saraf are the Chairman cum Director and Managing Director of ZIL, respectively. ZIL has two sets of businesses: Cloud Computing Business & Managed Services Business ('MSD').
3. The preliminary inquiry further revealed that ZIL had raised monies from foreign investors by issuing Foreign Currency Convertible Bonds ('FCCBs') of US\$ 33 million (₹ 179.19 crores) in August 2006 and those of US\$ 50 million (₹ 271.5 crores) in August 2007. The FCCBs were due for redemption in August 2011 and August 2012, respectively, as mentioned in ZIL's notice dated December 27, 2010.
4. On December 27, 2010, ZIL announced to BSE/NSE that its Board of Directors had resolved to raise funds for re-payment/redemption of FCCBs and for this purpose ZIL was calling an Extraordinary General Meeting (EGM) to obtain shareholders' approval to borrow money upto ₹ 1500 crore.

5. A resolution was passed by the shareholders of ZIL at its EGM held on January 29, 2011 approving and authorizing its Board of Directors to raise money for repayment/redemption of FCCBs in one or more of the following methods:

- a) *"To borrow moneys from Domestic markets and/or through External Commercial Borrowings up to an amount not exceeding ₹ 1,500 Cr.*
- b) *To sell and/or lease the business and/or divisions including the subsidiaries (wholly and partly) of the company and for that purpose to issue debt securities/ bonds, etc, in the domestic or international markets, as permitted by law....."*

ZIL submitted a copy of the approved resolution to the Exchange (NSE) on February 15, 2011.

6. On September 26, 2011, ZIL informed the BSE that :*"the Company have spun- off one Division of its Business known as MSD Division to M/s. Zenith Monitoring Services Pvt. Ltd. Mumbai which will be a Subsidiary of Zenith RMM LLC, by way of an Asset Purchase Agreement. However, Zenith Infotech Ltd. is going to be a major shareholder."*

7. During preliminary inquiry it was observed that despite realising money through the sale of its MSD Division, ZIL defaulted in the redemption of FCCBs as approved by its shareholders. Further, it failed to disclose to BSE/NSE the default in redemption of FCCBs. When on October 13, 2011, BSE *suo moto* sought clarification from ZIL, it informed BSE as under:

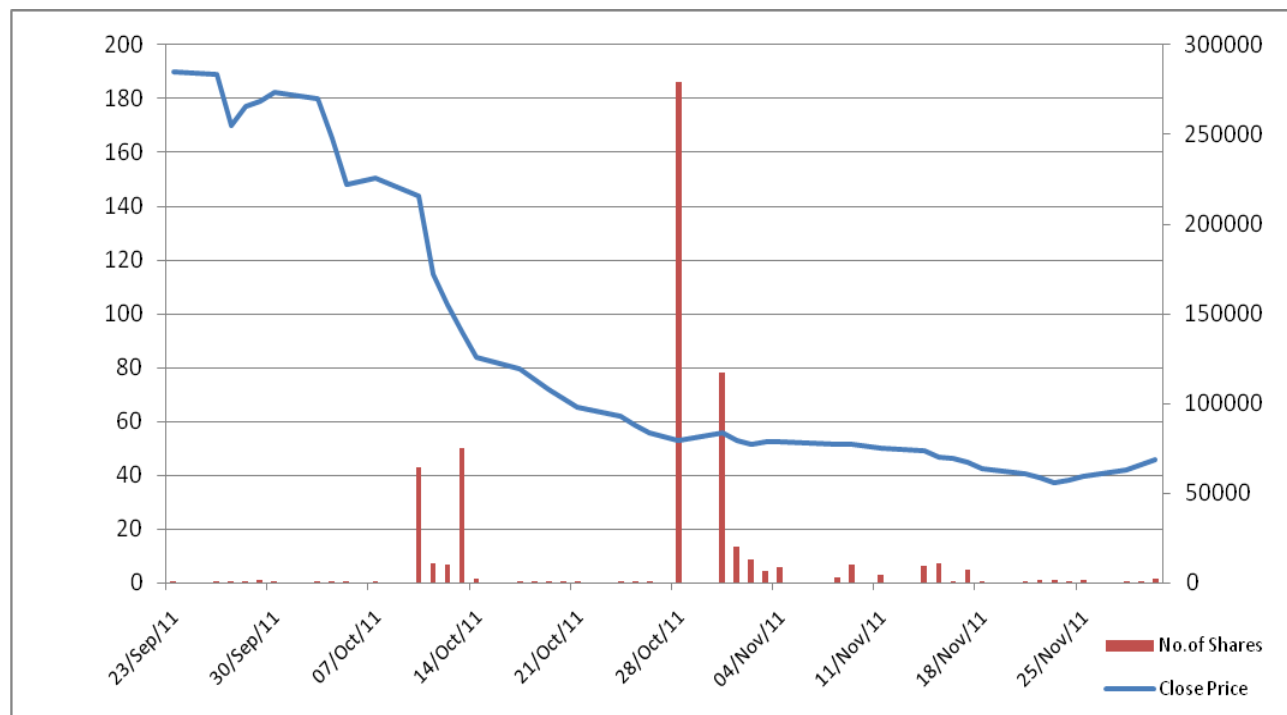
*"a. The company has defaulted on its US\$33mn FCCB which was due on 21st September 2011 and the company was (and is) in negotiations with the bondholders to extend the time for repayment.*

*b. As informed to BSE earlier vide our letter dated September 24th 2011, we have received all monies due from Zenith RMM, LLC except for the amount to be held in escrow, part of which the company plans to utilize for partial repayment of FCCBs.*

*c....."*

8. As news of probable default in redemption of FCCBs spread in the market, the share price of ZIL fell sharply from ₹190 on September 23, 2011 to approximately ₹45 on November 30, 2011 i.e. a fall of approximately 75% in just 45 trading days (as per BSE data). Even for the period from September 23, 2011 to October 13, 2011 (i.e. the day of disclosure of default on FCCBs by ZIL) the price of the scrip fell by half i.e. from ₹190 to ₹ 93. Further, it has been observed that the price of ZIL again halved to ₹ 45 on November 30, 2011. Moreover, it appears from the shareholding pattern that there was a marked decline in the shareholding of Institutional Investors from 20.17% to 11.96% during the quarter ending September 2011 to December 2011. The following graph demonstrates such fall in the price of the scrip.

**Price – Volume movement during the period September 23, 2011 to November 30, 2011**

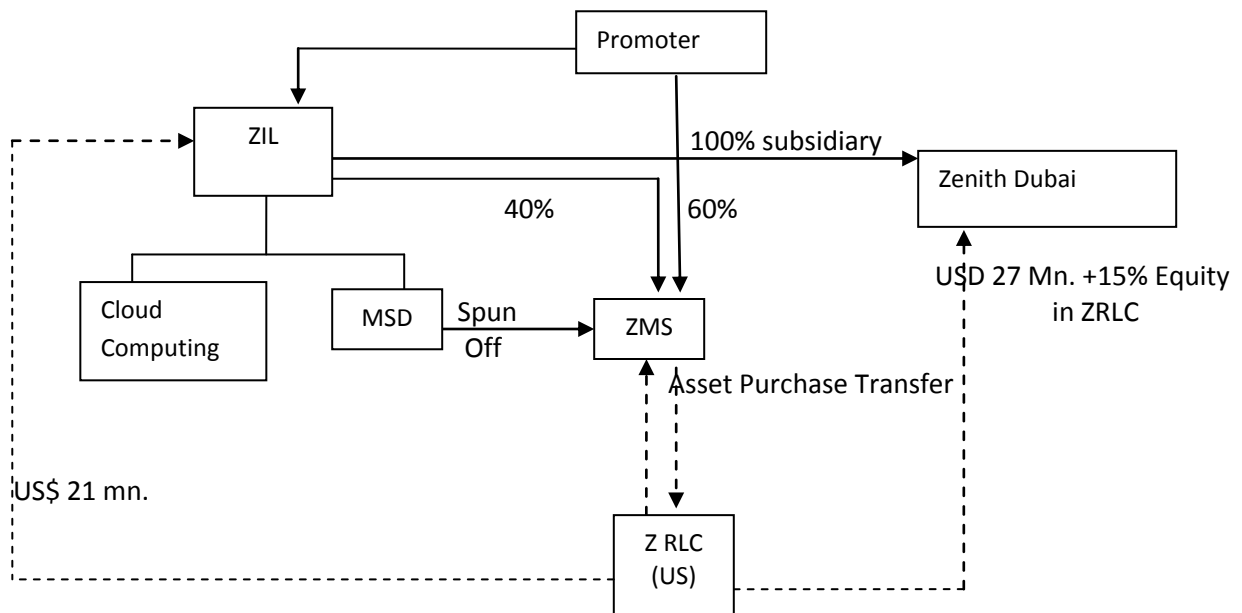


9. Vide letter dated December 10, 2011 ZIL submitted to SEBI that the matter of redemption of FCCBs is *sub judice* in a Suit(L) No. 3091 of 2011 before the Hon'ble High Court of Bombay. It further provided a copy of an affidavit dated November, 28, 2011 filed by Mr. Raj Kumar Saraf in the said Suit. ZIL has also submitted that it was in negotiations with the FCCB holders to make full or part payment or extend the maturity date. Further, ZIL stated that it did not make disclosure of the default as it would have prejudicially affected the interest of the company and its stakeholders. Yet the above price movements reveal that the uncertainty surrounding the event of redemption had, *prima facie*, substantially harmed the interest of the shareholders by the time of subsequent confirmation at BSE.
10. During the preliminary inquiry, the following sequence of the events in the case has been noted :
- ZIL spun-off one of its divisions, MSD, in a related party transaction to M/s. Zenith Monitoring Services Pvt. Ltd. Mumbai ('ZMS'), wherein Mr. Rajkumar Saraf and Mr. Akash Saraf (promoters of ZIL) hold 60% and 40% is held by ZIL.
  - Thereafter, Zenith RMM LLC ('ZRLC') a company based in USA entered into Assets Purchase Agreement with ZMS for buying MSD division. Later on ZRLC bought all the shares of ZMS thereby making it a subsidiary of ZRLC.
  - Consequent to the above arrangement, ZIL received consideration as under :
    - a monetary consideration of US\$54 million, out of which US\$6 million was kept in Escrow A/c (for any claims in the future); therefore, the cash received was US\$ 48 million; and

- ii. 15 % Equity stake in ZRLC, the value of which is approximately US\$ 7.4 million (as disclosed by ZIL).
- d) Out of the cash proceeds of US\$48mn;
  - i. ZIL received US\$ 21mn.
  - ii. The remaining amount of US\$ 27mn was given to a wholly owned subsidiary of ZIL, Zenith Infotech (FZE), based in Dubai, ('Zenith Dubai') as consideration for Software & Intellectual Property Rights of MSD Division held by it.
- e) The 15% equity stake in ZRLC, i.e. non-monetary part of the deal, was also issued in favor of Zenith Dubai.

11. The following chart demonstrates the above transactions:

**Chart showing the spinning-off transaction of MSD (Chart No. 1).**



12. Out of US\$21 million received by ZIL from the sale proceeds of MSD, US\$12.2 million was further transferred as follows:

- i. US\$ 3.2 million was given to Zenith Singapore (another wholly owned subsidiary of ZIL);
- ii. US\$ 6 million to other business creditors for goods and services supplied;
- iii. US\$ 3 million for capital goods for businesses of ZIL.

13. Out of US\$ 27 million received by Zenith Dubai from the sale proceeds of MSD Division, it transferred US\$ 21.73 million in the following manner:

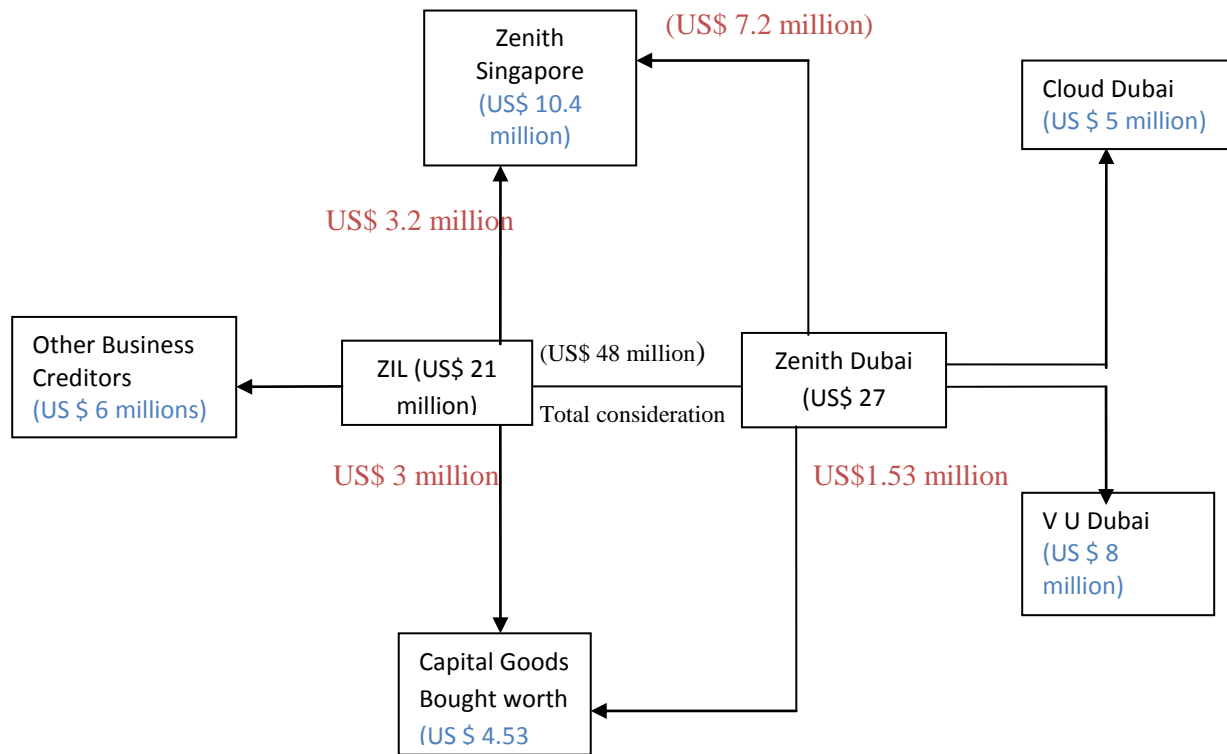
- a. US\$ 8 million was transferred to VU Telepresence FZC ('VU Dubai') and US\$ 5 million was transferred to Zenith Cloud Computing FZC, UAE ('Cloud Dubai'). These Dubai based entities are entities related to the promoters of ZIL and were categorized as “related parties” as

per the Annual Report 2011 of ZIL. However, on October 11 and 12, 2011 both companies were made subsidiaries of Zenith Dubai, which is in turn a subsidiary of ZIL.

- b. US\$ 7.2 million was moved to Zenith Singapore.
- c. US\$ 1.53 million was paid towards the purchase of capital goods.

14. The following chart demonstrates the payment of consideration as stated above:

**Chart showing the payment of consideration (Chart No. 2)**



15. From the above facts and circumstances revealed during preliminary inquiry, I note that out of the sale proceeds of MSD Division of ZIL (USD 48 million), an amount of USD 33.93 million was diverted for the purposes that were not even remotely connected to the authorization of the shareholders as under:-

- i. US\$ 13 million transferred to VU Dubai & Cloud Dubai;
- ii. US\$ 7.2 million and US\$ 3.2 million transferred to Zenith Singapore;
- iii. US\$ 1.53 towards purchase of capital goods by Zenith Dubai;
- iv. US\$ 6 million to business creditors of ZIL;
- v. US\$ 3 million for purchase of capital goods by ZIL.

The sequence of events and pattern of transactions in this case *prima facie* indicate that the ZIL and its promoters/directors not only wantonly defaulted in redemption of FCCBs and disregarded shareholders' resolution but also adopted fraudulent device and artifice to defraud the shareholders in view of the following facts and circumstances :

- (a) The two series of FCCBs issued by ZIL due for redemption in August 2011 and August 2012 had terms of cross default stipulating that default in redemption of FCCBs due in August 2011 would automatically cause a cross default on ZIL's obligation on the other series of FCCBs due for redemption in August 2012. ZIL and its promoters/directors, despite being fully aware of the terms of FCCBs and having approval of shareholders to redeem them, chose to divert the sale proceeds of MSD Division to their related entities.
- (b) The default with regard to redemption of FCCBs had occurred on September 21, 2011. ZIL and its promoters/ directors did not inform the BSE/NSE about failure to redeem the FCCBs and they tried to hide the information about default until intervention by exchanges on October 13, 2011.
- (c) The claim of ZIL, as submitted in its letters dated October 13, 2011 to BSE/NSE and December 10, 2011 to SEBI, that it was in negotiations with the FCCB holders to extend the time for redemption of FCCBs. It has been brought to SEBI's notice that FCCB holders have filed a suit against ZIL for recovery on October 21, 2011 and have also filed a winding up petition against ZIL. Thus, such disclosure by ZIL was *prima facie* false and misleading.
- (d) ZIL and its promoters/directors also failed to inform the exchanges and the shareholders about this material litigation against ZIL, thereby concealing this fact.
- (e) The disclosure, made on October 13, 2011 to BSE that ZIL planned to utilize sale proceeds of MSD Division for partial repayment of FCCBs is also false and misleading as the proceeds have not been used for this purpose at all. This disclosure also suggests misrepresentation of material fact of default of redemption.
- (f) The information about the amount of receipt of sale proceeds of MSD Division and the way in which it was utilized was concealed by ZIL and its promoters/directors. The fact that VU Dubai and Cloud Dubai were promoter related entities at the time of transfer of US\$ 13 million to them and were acquired to make them subsidiaries of ZIL was not disclosed to the stock exchanges, but came to notice of SEBI through complaints and media publications. ZIL and its promoters/directors did not seek the approval of shareholders for acquisition of these new companies, which was in contradiction to the original approval of the shareholders.
- (g) ZIL and its promoters/directors diverted the sale proceeds of MSD Division for myriad purposes other than that of redemption of FCCBs, as approved by its shareholders.
- (h) While examining the claim of ZIL regarding its financial soundness and ability to pay back FCCB holders, Hon'ble Bombay High Court, vide its order dated July 09, 2012 rejected the valuation of ZIL (cloud computing business) arrived at ₹ 598 crores and found the worth of ZIL to be in the range of ₹ 152- ₹ 211 crores only.

16. It appears from the above that ZIL and its promoters/directors through their decision and announcement dated December 27, 2010 made a promise to the shareholders without intending to perform the same. They diverted the monies realized from the sale of the MSD Division for the

benefits/interests of promoters and/or directors and subsidiaries. In my view, the terms of the FCCBs would have alerted any person of ordinary prudence to be more vigilant towards its redemption obligations as the default on such obligations normally results in the erosion of shareholders' value and more so in this case as the terms of FCCBs provided for cross default. I also do not see any compelling reasons to use the monies realized from sale of MSD Division for any purpose – not the least for paying to group entities for various purposes – other than for redemption of FCCBs, which was not only the sole purpose for which approval of shareholders was taken but was also very crucial for protecting the shareholders' value. The above facts and circumstances of the case, *prima facie*, indicate that the ZIL and its promoters/directors employed a device or artifice to fraudulently divert the sale proceeds of its MSD Division.

17. The aforesaid facts *prima facie* indicate that the acts, omissions and concealment of ZIL and its promoters /directors/ were 'fraudulent' as defined in regulation 2(1)(c) of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 ( PFUTP Regulations) which reads as under:-

***Definition of ‘fraud’ – Regulation 2(1)(c).***

*(c) “fraud” includes any act, expression, omission or concealment committed whether in a deceitful manner or not by a person or by any other person with his connivance or by his agent while dealing in securities in order to induce another person or his agent to deal in securities, whether or not there is any wrongful gain or avoidance of any loss, and shall also include—*

- (1) a knowing misrepresentation of the truth or concealment of material fact in order that another person may act to his detriment;*
- (2) a suggestion as to a fact which is not true by one who does not believe it to be true;*
- (3) an active concealment of a fact by a person having knowledge or belief of the fact;*
- (4) a promise made without any intention of performing it;*
- (5) a representation made in a reckless and careless manner whether it be true or false;*
- (6) any such act or omission as any other law specifically declares to be fraudulent;*
- (7) deceptive behaviour by a person depriving another of informed consent or full participation;*
- (8) a false statement made without reasonable ground for believing it to be true;*
- (9) the act of an issuer of securities giving out misinformation that affects the market price of the security, resulting in investors being effectively misled even though they did not rely on the statement itself or anything derived from it other than the market price.*

*And “fraudulent” shall be construed accordingly;*

.....”

18. In light of the aforesaid observations, it is *prima facie* established that ZIL and its promoters/directors not only failed to use the sale proceeds of MSD Division for the purpose authorized by the shareholders but have also taken away the assets of ZIL either for their own benefit or for that of the entities owned and controlled by them without authority of shareholders and in blatant disregard of their approval. In view of such observation, I, *prima facie*, find that the promoters/directors of ZIL

stripped the assets of ZIL for the benefit/interest of companies/entities controlled by them in fraudulent and deceitful manner which attracts prohibitions enshrined in section 12A (b) and (c) of the SEBI Act and regulation 3 (c) and (d) of the PFUTP Regulations which read as following:-

#### **Section 12A of the SEBI Act-**

#### **"Prohibition of manipulative and deceptive devices, insider trading and substantial acquisition of securities or control.**

*12A. No person shall directly or indirectly—*

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

*(c) engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person, in connection with the issue, dealing in securities which are listed or proposed to be listed on a recognised stock exchange, in contravention of the provisions of this Act or the rules or the regulations made thereunder;*

#### **Regulation 3 of the PFUTP Regulations -**

#### ***3. Prohibition of certain dealings in securities***

*No person shall directly or indirectly—*

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

*(d) engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person in connection with any dealing in or issue of securities which are listed or proposed to be listed on a recognized stock exchange in contravention of the provisions of the Act or the rules and the regulations made there under.*

19. The aforesaid apparent asset stripping of ZIL through a series of transactions for the purpose of benefitting the interests of its promoters /directors and related entities led to the following consequences:

- a. Shareholders/investors have lost considerable amount of money as a result of sharp price fall in the scrip of ZIL from approximately ₹190 on September 23, 2011 to approximately ₹45 on November 30, 2011 i.e. a fall of approximately 75% in just 45 trading days.
- b. The shareholders' value has eroded because of the misconduct of the promoters/directors as explained hereinabove.
- c. The company is still fastened with the liability to pay back the FCCB holders on account of redemption thereof. This will further have a financial burden on shareholders' wealth in ZIL.

20. I further note that the aforesaid acts and omissions on the part of the promoters/directors and the consequences thereof also raise the concerns about the non-observance of the principles of corporate governance. To this end, the Companies Act, the SEBI (Prohibition of Insider Trading) Regulations, 1992 (PIT Regulations) and the Listing Agreement provide various provisions to ensure equal treatment of shareholders and management in the listed companies. Relegating the interest of the



shareholders to a level subordinate to that of the management tantamounts to management failure in discharging their fiduciary duties towards the shareholders. The disclosure of material and price sensitive information serves as a tool for ensuring good management and governance of listed companies. With this objective, various disclosures requirements have been mandated in the Listing Agreement and PIT Regulations. As per clause 21 of the Listing Agreement, ZIL was under obligation to fix and notify BSE/NSE at least 21 days in advance the redemption date and amount payable on redemption of FCCBs and simultaneously issue cheques to them so as to reach them before the date of redemption. Clause 36 of the Listing Agreement and clause 2.1 read with clause 7.0 (ii) of Code of Corporate Disclosure Practices for Prevention of Insider Trading provided in Schedule II read with regulation 12(2) of the PIT Regulation obligated ZIL to immediately disclose the default in redemption of FCCBs since it was price sensitive information. In this case, ZIL and its promoters/ directors not only failed to honour the resolution as approved by its shareholders but also suppressed the price sensitive information. The submission of ZIL that the disclosure of default would have prejudicially affected the interests of its stakeholders cannot be accepted since in a disclosure based regime, the non-disclosure of material and price sensitive information as obligated by Listing Agreement and PIT Regulations would not only defeat the objective of regulations but would also adversely prejudice the interests of investors in securities market. It is also noted that ZIL failed to disclose the pending litigation between ZIL and the Trustee for the FCCB holders, as required under clause 36(5) of the Listing Agreement. As mentioned in Para 15 above, they also provided false and misleading disclosures to BSE which further strengthen the inference that the conduct of the promoters/directors in not utilizing the sale proceeds of MSD Division in accordance with the shareholders' approval was, *prima facie*, mala fide.

21. In light of the aforesaid *prima facie* findings, I note that the promoters/directors of ZIL have in a devious manner attempted to take away the assets of a listed company directly and indirectly for their own benefit or for benefit of entities owned and controlled by them. Such conduct of promoters / directors not only defeats the whole purpose of seeking shareholders' approval for crucial decisions but also jeopardizes the integrity of the securities market.
22. In my view, the above acts of ZIL and its promoters/directors, as brought out in the aforesaid paras, are *prima facie*, in violation of the following provisions of securities laws:
  - I. Section 12A (b) and(c) of the SEBI Act and regulations 3 (c) and (d) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003.
  - II. Clauses 21 and 36 of the Listing Agreement read with section 21 of Securities Contracts (Regulation) Act, 1956.
  - III. Clauses 2.1, and 7.0 (ii) of Code Of Corporate Disclosure Practices For Prevention Of Insider Trading provided in Schedule II read with Regulation 12 (2) of SEBI (Prohibition of Insider Trading) Regulations, 1992.

23. In the facts and circumstances of the case, it is necessary to take urgent action for the above violations so as to prevent further loss of shareholders' value due to stripping of the asset and erosion of value in ZIL and also to preclude reoccurrence of such defaults/ violations. It is also noteworthy that the conduct of ZIL and its promoters/directors may raise concerns about the integrity of the securities market and may tarnish the image and reputation of the Indian securities market amongst foreign investors which is bad for development of the markets.
24. Given the vital function of protecting investors and safeguarding the integrity of the securities market vested in SEBI and the commensurate powers given to it under the securities laws, it is necessary for SEBI to exercise these powers firmly and effectively to insulate the market and its investors from the fraudulent actions of the participants in the securities market. One of the basic premise that underlies the integrity of securities market is that the participants conform to standards of transparency, good governance and ethical behavior prescribed in securities laws and do not resort to fraudulent activities. In this case, the conduct of the promoters / directors, as brought out above has been violative of this basic premise. Therefore, in view of the aforesaid *prima facie* findings, it is felt necessary to intervene in this matter to safeguard the interest of the retail shareholders of ZIL and protect the integrity of the securities market. I am convinced that this is also a case where, pending investigation, effective and expeditious action is required to be taken to prevent any further harm to investors and to thwart any further design, which are *prima facie* fraudulent, manipulative and unfair, of ZIL and its promoters/ directors. This is also a fit case where SEBI needs to send a stern message to prevent companies and their promoters/ directors from indulging in such acts of omissions and commissions as observed in this case. In my view, therefore, in the facts and circumstances of this case an urgent preventive and remedial action needs to be taken by way of *ad interim ex -parte* order.
25. Therefore, in order to protect the interest of investors and the integrity of the securities market, I, in exercise of the powers conferred upon me by virtue of section 19 read with sections 11(1), 11(4) and 11B of SEBI Act, 1992 and section 12A of the Securities Contracts (Regulation) Act, 1956, pending investigation, hereby issue the following directions, by way of this *ad-interim ex-parte* order:
- i. The following promoters of ZIL are restrained from accessing the securities market and further prohibited from buying, selling or dealing in securities, directly or indirectly, in any manner whatsoever, till further directions :-

S. No.	Name	PAN Number
1.	Devita Rajkumar Saraf ( Promoter)	AAFPS8848D
2.	Vijayrani Rajkumar Saraf ( Promoter)	AMTPS0851J
3.	Zenith Technologies Pvt Ltd (Promoter)	AAACZ2074L
4.	Vu Technologies P Ltd (Promoter)	AACCV1663P
5.	Rajkumar Saraf (Promoter and Chairman cum Director)	AURPS4374C

6.	Akash Rajkumar Saraf (Promoter and Managing Director)	AAFPS8849C
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- ii. The board of directors of ZIL is hereby directed to furnish, within 30 days from the date of this order, bank guarantee(s) of a minimum tenure of one year, for USD 33.93 million (i.e. the amount of sale proceeds of MSD Division that has been diverted as described in para 15 above), in the name of Securities and Exchange Board of India, without using the funds of ZIL or creating any charge on assets of ZIL. The bank guarantee may be invoked in case any adverse inference is drawn by SEBI in its final order with regard to the actions of Board of directors/promoters of ZIL in diverting the sale proceeds of MSD Division and SEBI deems it necessary to compensate ZIL.
26. This order is without prejudice to the right of SEBI to take any other action that may be initiated against ZIL and its directors/promoters in accordance with law. The above directions are without prejudice to the rights of FCCB holders to enforce their rights of redemption against ZIL before competent authority, forum or court.
27. The persons/entities against whom this order has been passed may file their replies to SEBI within 21 days from the date of receipt of this order, if they so desire. They may also indicate in their replies whether they wish to avail an opportunity of personal hearing in the matter.
28. This order shall come into force with immediate effect.

**DATE: March 25<sup>th</sup>, 2013**  
**PLACE: Mumbai**

**RAJEEV KUMAR AGARWAL**  
**WHOLE TIME MEMBER**  
**SECURITIES AND EXCHANGE BOARD OF INDIA**