®

IN THE HIGH COURT OF KARNATAKA AT BANGALORE

ON THE 10TH DAY OF APRIL 2013

BEFORE

THE HON'BLE MR.USTICE K.L.MANJUNATH

AND

THE HON'BLE MR.JUSTICE RAVI MALIMATH

WRIT APPEAL NO.1178 OF 2008(GM-RES)

BETWEEN:

1. M/s.Guru Teak Investments (Mysore) Pvt.Ltd.,
   A Company incorporated under the provisions of
   Companies Act, 1956, having its Registered
   Office at No.874, Raineo House, 1st Floor,
   Dr.Modi Hospital Road,
   West of Chord Road,
   Bangalore – 560 086
   Represented through its Managing
   Director Mr.Gangadhar.

2. Mr.Gangadhar
   S/o Lingadevaraiah
   Aged about 47 years
   No.577, 3rd Cross, University Layout,
   Basaveshwaranagar,
   Bangalore. ...APPELLANTS

HIGH COURT OF KARNATAKA BANGALORE.

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(By Sri. Naganand, Senior Counsel, for M/s.Just Law, Advocates)

AND:

1. Union of India
   Represented Secretary to the
   Department of Finance,
   New Delhi.

2. Securities & Exchange Board of India
   Constituted under Securities Exchange
   Board of India Act
   1992 having its Office at Mittal Chambers
   Nariman Point
   Mumbai – 400 021 represented herein
   By its Chairman. ...RESPONDENTS

(By Sri Kalyan Basavaraj, ASG for R1
Sri S.Vijayashankar, Sr.Advocate for Sri Sudarshan Suresh, Advocate for M/s.King & Patridge, Advocates for R2)

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This Writ Appeal filed under Section 4 of the Karnataka High Court Act praying to set aside the order passed in the Writ Petition No.3922/2007 dated 8.7.2008

This Writ Appeal having been heard and reserved for judgment on 20.03.2013 coming on this day, Ravi Malimath J., pronounced the following:-

HIGH COURT OF KARNATAKA BANGALORE.

JUDGMENT

Aggrieved by the order dated 08.07.2008, passed by the Learned Single Judge in W.P. No.3922/2007, dismissing the petition, the petitioners have filed the present appeal.

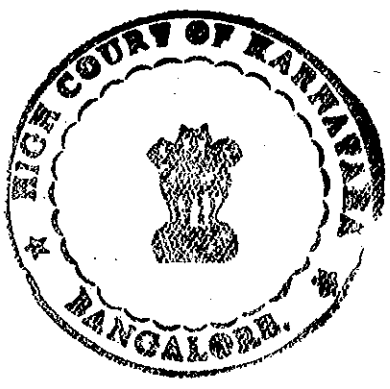
2. The first appellant was incorporated in the year 1996, under the provisions of the Indian Companies Act 1956. It is engaged in the business of Collective Investment Scheme (CIS) farming, Horticulture, Floriculture, etc., manufacture and sale of agro chemicals, to carry on business as timber merchants, to sell land with out without trees, plants, etc. The second appellant is a shareholder and the Managing Director.

3. The company made an application to the second respondent for registration under Section - 71(1) of SEBI (Collective Investments Scheme) Regulations

HIGH COURT OF KARNATAKA BANGALORE.

1999 (hereinafter referred to as 'Regulations'). A provisional registration under Regulation – 71, read with Regulation - 71(1) was granted subject to the conditions therein. One of the conditions was in terms of Regulation - 9(c), which states that the applicant should have a *'net worth'* of not less than Rs.5 crores. Hence, if that condition or any other condition was not fulfilled, the appellant would not be entitled for registration. The appellant was unable to comply with the same. Hence, a notice was issued as to why they should not be directed to wind-up the same and to repay the investors the amount received by them.

4. On hearing, an order was passed by the second respondent directing winding-up of the scheme. An appeal was preferred before the Appellate Tribunal. The Tribunal set-aside the order and remanded the matter to the second respondent for fresh disposal. Once again the appellant was heard. He could not



satisfy the condition at clause 9(c) of the Regulation. Therefore, they were directed to wind up the existing scheme and repay the investors. Aggrieved by the same, the appellant preferred an appeal before the Tribunal which was pending on the date of filing the writ petition.

5. In the interregnum, the appellant filed the instant writ petition seeking for a declaration that Regulation – 2(1)(s) of SEBI Regulation, 1999 is ultra vires Article – 14 of the Constitution of India, insofar as it excludes the funds created for revaluation while determining the *'net worth'* of the company and other reliefs. On contest, the Learned Single Judge by the impugned order, dismissed the writ petition. Hence, the present appeal by the petitioners.

6. Shri. Naganand, the learned senior counsel appearing for the appellants counsel contends that the impugned order is bad in law and liable to be set aside.

HIGH COURT OF KARNATAKA BANGALORE.

That in terms of the Regulations, the conditions imposed are unfair attracting Article – 14 of the Constitution of India. That the plea of the appellants on Article – 14 was not considered by the Learned Single Judge. That excluding the funds created for revaluation, has caused injustice to the appellants leading to miscarriage of justice by offending Article – 14. He contends that if the revaluation is taken into account, the *'net worth'* of the company would be far greater than Rs.5 crores, as stipulated in the Regulation. He therefore pleads that the writ be allowed and Regulation – 2(1)(s) be held to be ultra-vires Article – 14 of the Constitution of India.

7. On the other hand, the learned counsels appearing for the respondents defend the impugned order. They contend that there is no error committed by the Learned Single Judge. That the Learned Single Judge has rightly considered the contentions advanced.

HIGH COURT OF KARNATAKA BANGALORE.

That the Learned Single Judge was right in holding that the regulation is consistent and that there is no ambiguity which calls for any interference. Therefore, they plead that the appeal be dismissed

8. Heard learned counsels and examined the material on record.

9. The plea of the petitioner is to declare Regulation- 2(1)(s) as ultra-vires Article – 14 of the Constitution of India. That the conditions as stipulated in Regulation–9(c) would consequently be required to be set-aside.

10. Clause-2(1)(s) of the Regulation reads as follows:

> *"(s) 'net worth' means the aggregate value of the paid up equity capital and free reserved (excluding funds created out of revaluation), reduced by the aggregate value of accumulated losses and deferred expenditure*

HIGH COURT OF KARNATAKA BANGALORE.

not written off, including miscellaneous expenses not written off;"

11. The application for grant of a certificate is subject to the conditions as mentioned in Regulation–9. The conditions as mentioned in regulation–9 requires to be fulfilled. The grievances of the appellant is with reference to clause–(c) of Regulation–9, which reads as follows:

> ***"9. Conditions for eligibility**: The Board shall not consider an application for the grant of a certificate unless the applicant satisfies the following conditions, namely:*
>
> *(a) xxxxx*
>
> *(b) xxxxx*
>
> *(c) the applicant has a net worth of not less than rupees five crores;*
>
> *Provided that at the time of making the application, the applicant shall have a minimum net worth of rupees three crores*

HIGH COURT OF KARNATAKA BANGALORE.

which shall be increased to rupees five crores within three years from the date of grant of registration;

(d) xxxxx

(e) xxxxx

(f) xxxxx

(g) xxxxx

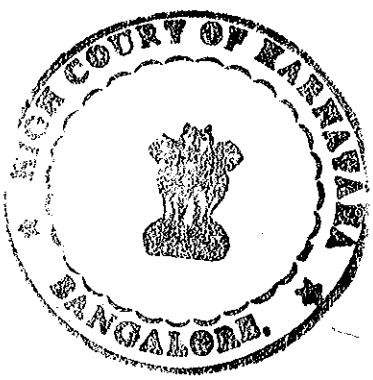
(h) xxxxx

(i) xxxxx

(j) xxxxx

(k) xxxxx"

12. Therefore, one of the conditions for eligibility is that the applicant should have a *'net worth'* of not less than Rs.5 crores, provided that at the time of making the application, the applicant shall have a minimum *'net worth'* of Rs. 3 crores, which shall be increased to Rs.5 crores, three years from the date of grant of registration. *'Net worth'* has been defined in Regulation - 2(1)(s). It narrates that *'net worth'* means - the aggregate value of the paid up equity capital and



free reserves excluding the funds created out of revaluation and reduced by the aggregate value of accumulated losses and deferred expenditure including miscellaneous expenses not written off. Therefore, the condition in regulation 9(c) is relatable to regulation 2(1)(s).

13. The Learned Single Judge while considering the contentions, compared the definition of *'net worth'* as enunciated in various other enactments. The definition of *'net worth'* under the Indian Companies Act and the Sick Industrial Companies (Special Provision) Act 1985 were considered. In terms of Section -2 (29-A) of the Companies Act and in terms of Section - 3(g)(a) of the Sick Industrial Act, the definition of *'net worth'* are identical. The Learned Single Judge also placed reliance on the judgment reported in *1993 (4) 392* in the case of *Commissioner of Income tax, Bombay and Others vs. Mahindra and Mahindra Limited and Others,* wherein

HIGH COURT OF KARNATAKA BANGALORE.

the meaning of *'net worth'* was explained. On so considering the same, the Learned Single Judge was of the view that in deciding the *'net worth'* of a company the market value can never be taken into consideration. That there is no scope for any interpretation by the Court regarding the aforesaid definition. The definition is simple, clear and unambiguous.

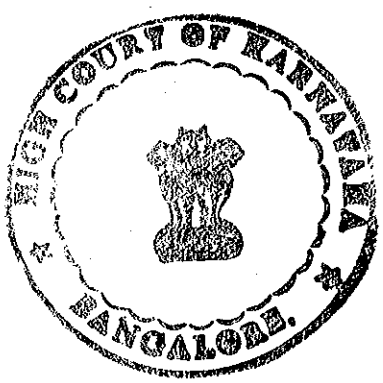
14. On considering the reasonings of the Learned Single Judge, we are of the considered view, that there is no error committed by the Learned Single Judge that calls for interference. The definition of *'net worth'* as contained in the Companies Act, as well as the Sick Industries Act are *pari materia*. That the definition of 'networth' in these two enactments has stood ground. Hence, we find no good ground to hold that only so far as the definition of *'net worth'* in these regulations is concerned, it is arbitrary. It is unacceptable. The writ petition was rightly dismissed.

HIGH COURT OF KARNATAKA BANGALORE.

15. However, the learned counsel for the appellants contends that his contention on the violation of Article-14, was not considered by the Learned Single Judge. There is no reference to his contentions. Hence, arguments were advanced on the same. He contends that the accounts of the company are maintained in accordance with law as per Section–209 to 215 of the Companies Act 1956, which have been audited by the Companies Auditors. That there is no provision under the Companies Act or in the Accounting guidelines issued by the Institute for Chartered Accountant of India, that the assets of the company should not be revalued. That it is a well settled principle of accounting, that the balance-sheet should truly and fairly reflect the value of the assets. That the petitioner owns a large extent of 1272 acres. The teak trees planted are in a portion of the land to an extent of 400 acres. The petitioner company valued the standing

HIGH COURT OF KARNATAKA BANGALORE.

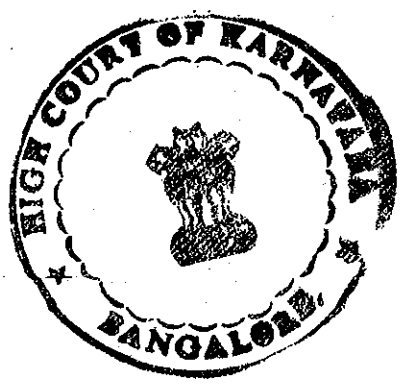
timber. The value was found significantly higher than the balance sheet figures and therefore after making a conservative assessment, the standing timber was revalued and brought to books. These revaluations have now resulted in the balance sheet of the company reflecting the true value of a portion of its assets. That such a revaluation far exceeds the requirements of regulation-9(c). That the *'net worth'* of the company as on September'2005 was Rs.53.49 crores in terms of the valuation issued by the Chartered Accountant and the registered valuer. Further, Regulation–9(c) prescribes the condition for eligibility. That the eligibility excludes the funds created out of revaluation. Therefore, this condition is unreasonable. That the compliance in terms of the definition of *'net worth'* is arbitrary and violation of the Article – 14 of the Constitution Of India. By such an artificial definition, the right of the petitioner to carry on its business guaranteed by Article–19, is



consequently affected. As such, the definition has no nexus with objects sought to be achieved. Hence, it is pleaded that the writ be allowed by declaring Regulation-2(1)(s) as ultra-vires Article–14 of the Constitution of India.

16. On the other hand, the learned counsel for the respondents defend the Regulation. It is contended that the regulation does not offend Article – 14 nor the fundamental right of the petitioner under Article–19 of the Constitution of India. That the right to carry on business has not been denied. That the plea of infringement of Article–14 is misplaced.

17. On hearing learned counsels, we are of the considered view that the contentions put forth on Article–14 are unacceptable. We do not find any infringement of Article-14. The Regulations are made in exercise of the powers conferred under Section–30, read



with Sections – 11 and 19 of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as 'Act'). The Act was promulgated to provide for the establishment of a Board, to protect the interests of the investors in securities and to promote development of and to regulate the securities market and for matters connected with or incidental thereof. Chapter–4 of the Act enumerates Sections – 11 to 11D. They relate to the powers and functions of the Board. That is shall be the duty of the Board to protect the interest of the investors in securities, to promote development and to regulate the securities market by such measures as it thinks fit. Various provisions have been enacted to provide for such measures. Section–30 confers the power on the Board to make regulations consistent with the Act to carry out the purposes of the Act. It is under these provisions that the regulations have been formed. The regulations would state that - no person other than a

HIGH COURT OF KARNATAKA BANGALORE.

Collective Investment Management Company, which has obtained a certificate of registration under the SEBI (Collective Investment Scheme) Regulations, 1999, shall carry on or sponsor or launch a Collective Investment Scheme. Also, no Collective Investment Scheme shall be launched or any new scheme to raise money from the investors even under the existing schemes, unless a Certificate of Registration is granted to it under the said Regulations.

18. The grant of the certificate is subject to the conditions in Regulation-9. Therefore, the Act and Regulations are intended to promote the orderly and healthy growth of the securities market, for investors protection etc. Therefore, various powers and duties are vested with the Board to effectively deal with the capital markets. Under these circumstances, the grant of certificate is necessarily, subject to the conditions as

HIGH COURT OF KARNATAKA BANGALORE.

mentioned in Regulation-9. Therefore, if the conditions are not fulfilled, the applicant would not be entitled for such a certificate.

19. As a result of the conditions prescribed in the Regulations, the objects of the Act are sought to be achieved, namely to promote an orderly healthy growth of the market and for investors protection etc. It is in pursuance of the objects sought to be achieved, that the regulations prescribe, the conditions for eligibility for a certificate, wherein the applicant should have a *'net worth'* of not less than Rs.5 crores. The exclusion of funds created out of revaluation in terms of the definition of Regulation–2(1)(s), cannot be said to be arbitrary or an artificial definition. The object sought to be achieved in defining *'net worth'* to exclude the funds created out of revaluation, is to protect the interest of the investors. The protection of the interests of the investors is sought to be achieved by defining *'net*

HIGH COURT OF KARNATAKA BANGALORE.

worth', which means the aggregate capital and free reserves and excluding the funds created out of revaluation. The funds created on revaluation would at times amount to an artificial valuation and not the true value. That the interest of the investors would necessarily be affected if *'net worth'* includes such revaluation. Therefore, *'net worth'* has been defined to exclude such a revaluation. Such a definition in our considered view is just, fair and reasonable. That by defining *'net worth'*, the object sought to be achieved is the protection of the interests of the investors etc. Therefore there is a nexus with the regulation and the object sought to be achieved. Hence, the contention of arbitrariness by offending Article–14 or the right to do business under Article-19(1)(g) is unsustainable.

20. It is presently submitted at the Bar that aggrieved by the order dated 8.2.2006, an appeal in appeal No.48/2006 was filed before the Securities

HIGH COURT OF KARNATAKA BANGALORE

Appellate Tribunal. which was pending as on the date of filing of the writ appeal. However, by the order dated 29.8.2008, the Tribunal dismissed the appeal and held that the appellant should wind up the scheme according to the provision of the regulations and repay the investors in accordance with the Regulation – 73 and other directions were issued.

21. However, it is further submitted by the respondent, that this order of the Tribunal was questioned by filing Civil Appeals No.326/09 before the Hon'ble Supreme Court, wherein by the order dated 2.4.2009, the civil appeal was dismissed keeping open the question of law.

22. Therefore, for the aforesaid reasons, we find no error committed by the Learned Single Judge that calls for interference on merits, Law and facts. That the

HIGH COURT OF KARNATAKA BANGALORE.

order of the Learned Single Judge is well reasoned and does not call for any interference. The grounds urged by the appellants on Article – 14 and that it was not considered by the Learned Single Judge, has since been considered at length in the aforesaid paragraphs.

23. For the aforesaid reasons, we are of the considered view that there is no merit in the appeal. We do not find any error in the order of the Learned Single Judge that calls for interference. Consequently, the appeal being devoid of merits is dismissed.

HIGH COURT OF KARNATAKA BANGALORE.

Sd/-
JUDGE

Sd/-
JUDGE

JJ

a) The date on which the application was made 10.4.13
b) The date on which charges and additional Charges if any, are called for .....
c) The date on which charges and additional Charges, if any are deposited/paid 18.4.13
d) The date on which the copy is ready
e) The date of notifying that the copy is ready For delivery 18.4.13
f) The date on which the applicant is required to appear on or before 22.4.13
g) The date on which the copy is delivered to the Applicant 19/4/13
h) Examined by .....

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18/4/13
Section Officer,
High Court of Karnataka.
Bangalore - 560 001.