BEFORE THE ADJUDICATING OFFICER

SECURITIES AND EXCHANGE BOARD OF INDIA

[ADJUDICATION ORDER/SS/AS/2019-20/6280]

UNDER SECTION 15-I OF THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 READ WITH RULE 5 OF THE SEBI (PROCEDURE FOR HOLDING INQUIRY AND IMPOSING PENALTIES BY ADJUDICATING OFFICER) RULES, 1995.

In respect of:

ICRA Limited
(SEBI Registration No. IN/CRA/008/15)
Building No. 8,2nd Floor, Tower A,
DLF Cyber City, Phase II,
Gurgaon - 122 002

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1. ICRA Limited (hereinafter referred to as 'ICRA'/ 'Noticee') is a '*credit rating agency*' registered with Securities and Exchange Board of India ('SEBI') under the SEBI (Credit Rating Agencies) Regulations, 1999 (hereinafter referred to as 'CRA Regulations') bearing SEBI Registration No. IN/CRA/008/15.

2. By a common *communication-order* dated March 25, 2019, this case pending before an erstwhile Adjudicating Officer appointed to conduct inquiry and adjudication against the Noticee, has been transferred to the undersigned with an advice that except for the change of the Adjudicating Officer, the other terms and conditions of the original orders *'shall remain unchanged and shall be in full force and effect'*. The records of these proceedings were provided to undersigned on April 05, 2019.

3. On receipt of records, it was noted that on being *prima facie* satisfied that there are sufficient grounds to inquire and adjudicate certain alleged violations of the provisions of the CRA Regulations by the Noticee. SEBI, vide a *communication - order* dated December 13, 2018, appointed, under section 15I of the SEBI Act its officer Shri Suresh B. Menon, Chief General Manager ('erstwhile AO') as adjudicating officer to inquire and adjudge under Rule 3 of the SEBI (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules, 1995 (Adjudication Rules) and section 15HB of the SEBI Act, the alleged violations of the provisions of Regulation 24(7) and Clauses 4 and 8 of Code of Conduct for the '*credit rating agencies*' read with Regulation 13 of the CRA Regulations. The text of the provisions of Regulations 13, 24(7) and Clauses 4, and 8 of Code of Conduct of the CRA Regulations and provisions of section 15HB of the SEBI Act are reproduced as following :-

Code of Conduct

Regulation 13 *- Every credit rating agency shall abide by the Code of Conduct contained in the Third Schedule.*

24(7) *- Every credit rating agency, shall, while rating a security, exercise due diligence in order to ensure that the rating given by the credit rating agency is fair and appropriate.*

CODE OF CONDUCT FOR CREDIT RATING AGENCIES

4. A credit rating agency shall at all times exercise due diligence, ensure proper care and exercise independent professional judgment in order to achieve and maintain objectivity and independence in the rating process.

8. A credit rating agency shall keep track of all important changes relating to the client companies and shall develop efficient and responsive systems to yield timely and accurate ratings. Further a credit rating agency shall also monitor closely all relevant factors that might affect the creditworthiness of the issuers.

SEBI Act

Penalty for contravention where no separate penalty has been provided.

15HB. *Whoever fails to comply with any provision of this Act, the rules or the regulations made or directions issued by the Board thereunder for which no separate penalty has been provided, shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one crore rupees.*

4. The erstwhile AO had issued the notice to show cause no. SEBI/EAD-1/SBM/34473/2018 dated December 17, 2018 ('the SCN') to the Noticee in terms of Rule 4(1) of the Adjudication Rules read with section 15I of the SEBI Act, calling upon the Noticee to show cause as to why an inquiry should not be held against it in terms of Rule 4 of the Adjudication Rules and penalty be not imposed under section 15HB of the SEBI Act upon it for the aforesaid alleged violations. The charge in the SCN was leveled in view of the following observations/ findings observed by SEBI during its examination-

A. On account of default committed by Infrastructure Leasing & Financial Services Limited (hereinafter referred to as 'IL&FS' / 'Issuer') and its subsidiary company IL&FS Financial Services Ltd. (hereinafter referred to as 'IFIN') on their obligations in respect of the Commercial Paper ('CP'), inter-corporate deposits ('ICD') and also default on interest payments on its Non-convertible Debentures(NCDs'), SEBI undertook an examination with respect to the role of the Credit Rating Agencies ('CRAs'), including the Noticee in assigning rating to various NCDs of IL&FS. It was observed that IL&FS had defaulted on its obligations in respect of the CP and ICDs which were due for payment on September 14, 2018. The said CP was rated by the Noticee

amongst other CRAs. Subsequently, IL&FS also defaulted in the interest payments on its NCDs on various dates i.e. September 17, 21, 26 and 29, 2018.

B. SEBI observed that the Noticee had downgraded the ratings of the NCDs issued by IL&FS on various occasions as follows:

Date	Rating assigned by Noticee
March 27, 2018	Reaffirmed at AAA
Aug 06, 2018	Downgraded from AAA to AA+.
Sept 08, 2018	Downgraded from AA+ to BB.
Sept 17, 2018	Downgraded from BB to D.

C. SEBI, in its assessment of the role of the Noticee in assigning the aforementioned ratings at various stages, alleged the following deficiencies on the part of the Noticee: -

I. **Allegation regarding excessive reliance placed by the Noticee on the submissions of the management of IL&FS**

a. The Noticee had placed excessive reliance on the information provided by the Management of IL&FS with regard to updates on the status of implementation of various projects / deals / fund raising plans such as signing of agreement, decisions made during its board meetings etc. and failed to carry out independent due diligence to ascertain the veracity of the updates provided by the management of IL&FS. The Noticee also failed to keep track of the various disclosures available on the website of BSE, as made by IL&FS from time to time.

b. From the information provided by IL&FS to the Noticee vide email dated August 02, 2018, it was observed that the Board of Directors of IL&FS, in its meeting held on July 21, 2018, approved equity infusion up to ₹4500 crore by way of rights issue. Further, IL&FSin the disclosure made to BSE, had disclosed about the resignation of Mr. Ravi Parthasarthy and appointment of Mr. Bhargava as its Non-Executive Chairman but had not disclosed the approval of the aforesaid equity infusion up to ₹4500 crore by way of rights issue.

c. From the Press Release dated August 29, 2018 of IL&FS available on its website, it was observed that its Board of Directors had, in the meeting dated August 29, 2018, *inter alia*, approved a *'rights issue'* amounting to ₹4500 crore and '*specific asset divestment plan'* to reduce the overall debt by ₹30,000 crores. A copy of the said Press Release was also forwarded to the Noticee by IL&FS. However, in the disclosure made to BSE with regard to the outcome of

the said board meeting, IL&FS had only disclosed information regarding approval of fund raising by way of Public Issue of Secured Redeemable NCDs, for an amount not exceeding ₹50 Billion, of which there was no mention in the aforesaid Press Release.

d. It was alleged that the abovementioned disparity in the disclosures made by IL&FS in its Press Release and the information submitted to BSE had, *prima facie*, warranted greater due diligence and care on the part of the Noticee in order to ascertain the veracity of the updates provided by the management of IL&FS to the Noticee. However, the Noticee failed to take note of the abovementioned disparity in the disclosures made by IL&FS.

e. From various rating committee notes it was observed that, despite the declining financial indicators of IL&FS *viz*. the stressed balance sheet, asset-liability mismatch, debt to equity ratio being predominantly negative, the Noticee continued to assign the highest possible rating (AAA) to the NCDs issued by IL&FS, based mainly on institutional parentage of IL&FS and the assurances given by IL&FS management to the Noticee from time to time. In view of the same, it was alleged that the Noticee had failed to exercise proper due diligence by way of independent confirmation of various claims made by the management of IL&FS which ultimately led to misrepresentation of financial health of IL&FS in the eyes of the investors.

II. **Allegation regarding failure to change the Rating Outlook or place the rating under Credit Watch**

a. The Noticee had maintained the Rating Outlook on the NCDs of IL&FS as '*Stable*' throughout the rating period despite the slow pace at which the asset monetization and deleveraging steps of IL&FS was taking place. The rating rationales given by the Noticee on January 03, 2018 and March 27, 2018 shows that the Noticee has given the outlook as '*Stable*' despite stating that the outlook might turn negative if, *inter alia*, there is significant deviation in the execution of divestment plans which would impact its deleveraging plans. The rating committee notes dated March 31, 2016, March 31, 2017, October 27, 2017 and March 23, 2018 that IL&FS had provided the timeline for monetisation of its various projects. From the perusal of the aforesaid plan submitted by IL&FS to the Noticee, it is observed that some projects like signing Power Purchase Agreement (PPA) by Unit II of Cuddalore Power Plant, sale of YuHe Expressway and IL&FS Securities Services were in pipeline since March 2016 and there was no sign of completion of these projects even in March 2018. Further, the plan of launching InvITs by IL&FS, which was communicated by the IL&FS to the Noticee in March 2017, was also put on hold for one year. Thus, it was alleged that the Noticee despite being aware of the

aforementioned facts indicating inordinate delays in monetisation of assets by IL&FS/ generating cash flows, maintained the outlook for the debt instruments of IL&FS as stable. It was also alleged that the Noticee had failed to adequately caution the investors regarding the high leverage and delay in implementation of asset monetization plans by IL&FS as it was waiting for further deviations to turn the outlook to negative. In view of the above, it was alleged that the Noticee had not exercised proper care and diligence and shown the prudence expected from a '*credit rating agency*'.

b. It is further observed that the ratings were placed under "*Watch with developing implications*" only in August 06, 2018, while downgrading the rating to AA+. In view of the same, it was alleged that the Noticee had failed to exercise its duty to the investors at large and failed to intervene in the matter on time by downgrading the ratings of NCDs of IL&FS despite having a knowledge of the deteriorating financials of the issuer.

III. **Allegation regarding failure to consider latest financials in the rating committee note presented on October 27, 2017.**

a. It was observed that while rating the facilities of IL&FS during the period August – October 2017, the Noticee had sought certain figures *viz*, top 15 loans and advances, top 20 investments, total contingent liabilities, segment wise breakup of borrowings as on June 30, 2017, and the same was provided to the Noticee by IL&FS vide email dated August 14, 2017. It is also observed from the figures provided by IL&FS that the borrowings of IL&FS had increased from ₹12,122.20 crore on March 31, 2017 to ₹13,113.10 crore as on June 30, 2017. However, it was alleged that these figures were not presented by the Noticee to its rating committee in the note presented on October 27, 2017 and were also not disclosed in the Rating Rationale dated November 3, 2017.

b. Further, the Noticee had not provided any e-mail wherein it had sought updated figures for Asset Liability Mismatch (ALM), as on June 30, 2017. Vide email dated September 20, 2017, IL&FS has submitted ALM as on March 31, 2017 and ICRA has presented the same to its rating committee. It is alleged that Noticee did not make efforts to seek ALM profile as on June 30, 2017, which was the most important point of analysis considering that the business of NBFCs/ CICs depends on their ability to maintain a comfortable asset – liability position across various buckets. Therefore, it was alleged that the Noticee had not exercised prudence and due diligence by not ascertaining/analysing the ALM position of IL&FS, as on June 30, 2017.

IV. **Observations of Reserve Bank of India with regard to the rating done by the Noticee of the CPs of IL&FS and IFIN.**

It was observed that the Noticee, being an agency empanelled by Reserve Bank of India (**RBI**), had also rated the CPs issued by IL&FS. In this regard, it was observed that the Noticee had downgraded the CPs, issued by IL&FS and IFIN, from A1 (highest possible rating) to A4 (least possible rating) in its rating outlook dated September 08, 2018 in one go. In this regard, RBI, vide its letter dated November 22, 2018 had given the following observations: -

a. *The CRAs had derived comfort from the institutional parentage of IFIN. An independent assessment of IFIN by the CRAs as a standalone entity with specific focus on the effectiveness of the prevailing governance systems and executive capability is not evidenced from the clarifications furnished. Further, there is a clear gap in identifying the ultimate major shareholders in case of such diversified ownerships, who might take a call on critical issues during such adverse situations.*

b. *IFIN derived financial flexibility and resource raising ability solely by virtue of IL&FS parentage. Besides these, the treasury and risk management function was shared by IFIN with the parent entity. The CRAs could have also evaluated the structure of IFIN on a standalone basis to gauge the finer aspects of degree of reliance on group entities and vice versa. Further, sharing of core business functions like treasure and risk management by group entities may be a desirable set-up, as the same may have adverse externalities during a system-wide contagious event. The group risk aspects were not examined by the CRAs.*

c. *The CRAs derived comfort from the liquidity profile of IFIN for positions as on March 31, 2017 and March 31, 2018 which generally reflected positive cumulative mismatches across time buckets for the short and medium term time horizons except for a cumulative mismatch of* Rs. *482 crores in the 1-2 months' bucket as on March 31, 2018. In addition to this, unutilized working capital limits and undrawn bank lines aggregating to* Rs. *1151 crores and* Rs.*812 crores as on March 31, 2017 and March 31, 2018 respectively facilitated a better perception of the liquidity position of the entity amongst the CRAs. However, the expansion in exposure of IFIN to group entities during FY 2017-18 (by 33.14%) through transitory loans extended in order to accommodate the delay in disbursements from banks/ FIs were not examined by the CRAs from the perspective of repayment capability.*

d. *The rating reliance was more on the commitments provided by the management on gradual reduction of such group exposures through monetizing and refinancing of these project debts at the underlying SPVs as well as the access to the shares treasury infrastructure of IL&FS by IFIN which failed to materialize beneficially.*

e. On account of mere initiation of a few measures by IFIN's management, the rating downgrade was effected by only one notch from AAA to AA+ by CARE on August 16, 2018 despite several critical issues. Further, relying on the reasons stated by IFIN for delay as technical in nature, no downgrade was initially effected by ICRA on the rating assigned to CPs. Subsequently, even though the same was recognized as a material event, the rating was not downgraded and continued to be A1+ as on September 3, 2018.

f. Most of the loans extended by IFIN were in respect of high ticket promoter funding and infrastructure loans with long gestation periods. Although the top 15 individual borrowers constituted around 30% of the total credit exposure of IFIN, the same was not examined by the CRAs from the perspective of concentration risk."

5. In view of the above, SEBI found that the Noticee, while assigning its '*credit rating*' to the NCDs of IL&FS, failed to exercise proper skill, care and due diligence while discharging its responsibilities as a '*credit rating agency*'. It was also found that the Noticee, being a responsible '*credit rating agency*' registered with SEBI, should have anticipated the mounting credit risks, the stressed balance sheet position of the issuer and placed the '*ratings'* accordingly to alert the market in advance regarding the deteriorating financial profile of the issuer. In view of the above, the Noticee is alleged to have violated the provisions of Regulations 13, 24(7) and Clauses 4 and 8 of Code of Conduct of the CRA Regulations.

6. Vide its reply dated January 02, 2019 the Noticee had made request before the erstwhile AO for inspection of entire relevant records including the material that would support the charges and those which will undermine the charges. The erstwhile AO, vide letter dated January 03, 2019 had informed the Noticee that, its request for inspection of relevant records/documents was forwarded to the Enforcement Department of SEBI. Pending inspection of relevant records/documents, the Noticee had not filed its reply to the SCN on merits.

7. On March 28, 2019, the Settlement Division of SEBI had informed erstwhile AO that the Noticee had filed settlement application under the SEBI (Settlement Proceedings) Regulations,2018 ('Settlement Regulations') seeking to settle the instant proceedings by settlement order and had advised him to keep the instant proceedings on hold till the disposal of the settlement application of the Noticee.

8. Thereafter, vide its letter dated April 03, 2019, the Noticee had informed the erstwhile AO that pursuant to its preliminary inspection of the records on February 08, 2019, vide its e-mail dated February 12, 2019 and March 01, 2019, it had sought certain additional documents from the Enforcement Department of SEBI for completion of the inspection process. The Noticee was awaiting the receipt of such additional documents from the Enforcement Department of SEBI and it will file the reply to the SCN on completion of the inspection of documents. It was noted that the

instant proceedings were kept on hold in view of the pendency of the settlement application of the Noticee.

9. On July 03, 2019, the Settlement Division of SEBI informed about the rejection of the settlement application of the Noticee in terms of Regulation 5(4) of the Settlement Regulations and requested undersigned to proceed with the instant proceedings. Accordingly, on July 10, 2019 the Enforcement Department of SEBI was requested to dispose of the requests of the Noticee made by its e-mails dated February 12, 2019 and March 01, 2019 regarding additional documents pursuant to inspection of relevant records.

10. Thereafter, on receiving the additional documents from Enforcement Department of SEBI and disposal of the Noticee's request on August 16, 2019, the Noticee vide its letter dated September 17, 2019, filed its reply to the SCN in the matter.

11. Vide notice dated September 19, 2019 the Noticee, was provided an opportunity of personal hearing in terms of Rule 4(3) of the Adjudication Rules on October 01, 2019.After seeking short adjournment, the Noticee availed the opportunity of hearing on October 03, 2019, when Shri Somsekhar S.,advocate appeared on behalf of the Noticee and made submissions on the basis of Noticee's reply dated September 17, 2019 and referred to several provisions of the CRA Regulations to point out the view of the Noticee on the overview of the CRA Regulations. He pithily stated that '*rating'* as defined under Regulation 2(1)(q) of the CRA Regulations is merely an opinion regarding securities expressed in the form of standard symbols. The Noticee has freedom of expression and investor is not precluded from doing his own due diligence. He also referred to several submissions made in respective paragraphs of the reply of the Noticee. Due to paucity of time on account of his busy schedule the arguments could not be completed and as requested by the Learned Advocate the next date was fixed on October 11, 2019, when the Learned Advocate of the Noticee appeared and filed and *Aide Memoires* for arguments and concluded his arguments based on the reply of the Noticee and relied upon case laws *viz;* Order of Hon'ble Securities Appellate Tribunal (SAT) dated June 03, 2019 in the matter of *Brickwork Rating India Limited V's SEBI in appeal No. 439 of 2018, para 6-9* and Order of Hon'ble Supreme Court dated March 14,2018 in the matter of *Chintalapati Srinivasa Raju v. SEBI, Civil Appeal No. 16805 of 2017, Paras 17 and 21* to buttress his point.

12. The replies and submissions of the Noticee are summarized *inter alia* as under: -

A. <u>With regard to Regulatory overview</u>: -

I. The concept of "*rating*" is defined in regulation 2(1)(q) of the CRA Regulations "*means an* ***opinion*** *regarding securities, expressed in the form of standard symbols or in any other* ***standardised manner****, assigned*

by a credit rating agency and used by the issuer of such securities, to comply with a requirement specified by these regulations;". Thus, '*rating*' is defined in the Regulation 2(1)(q) as an '*expression*' of an '*opinion*' in a '*standardised form*'. Thus, it is not a statement of fact, which can be objectively challenged. Expression of such opinion i.e. '*rating'*, is part and parcel of the freedom of speech and expression subject to reasonable restriction as envisaged under Article 19(l)(a) of the Constitution of India. Therefore, a rating agency has freedom of expression subject to the law laid down under Regulations framed under the SEBI Act. The Indian regulations are subject to *'reasonable restrictions'*. That is, expression of an opinion must be reasonable and logical.

II. The framework under the CRA Regulations, as set out in Regulations 13 to 16, 24, 29 and the Code of Conduct contained in the Third Schedule are extracted below:

"***Code of Conduct***

13. Every credit rating agency shall abide by the Code of Conduct contained in the Third Schedule.

Agreement with the Client

14. Every Credit rating agency shall enter into a written agreement with each client whose securities it proposes to rate, and every such agreement shall include the following provisions, namely:

(d) ***the client shall agree to co-operate with the credit rating agency in order to enable the latter to arrive at, and maintain, a true and accurate rating of the client's securities and shall in particular provide to the latter, true, adequate and timely information for the purpose.***

Monitoring of ratings

15.(1) ***Every credit rating agency shall, during the lifetime of securities rated by it continuously monitor the rating of such securities,*** *unless the rating is withdrawn, subject to the provisions of regulation 16(3).*

(2) Every credit rating agency shall disseminate information regarding newly assigned ratings, and changes in earlier rating promptly through press releases and websites, and, in the case of securities issued by listed companies, such information shall also be provided simultaneously to the concerned regional stock exchange and to all the stock ' exchanges where the said securities are listed.

Procedure for review of rating

16. (1) ***Every credit rating agency shall carry out periodic reviews of all published ratings during the lifetime of the securities,*** *unless the rating is withdrawn, subject to the provisions of regulation 16(3).*

(2) ***If the client does not co-operate*** *with the credit rating agency so as to enable the credit rating agency to comply with its obligations under regulation 15 of these regulations, the credit rating agency shall carry out the review on the basis of the best available information or in the manner as specified by the Board from time to time. Provided that if owing to such lack of co-operation, a rating has been based on the best available information, the credit rating agency shall disclose to the investors the fact that the rating is so based.*

(3) A credit rating agency shall not withdraw a rating so long as the obligations under the security rated by it are outstanding, except where the company whose security is rated is wound up or merged or amalgamated with another company, or as may be specified by the Board from time to time.

Rating process

24. (1) ***Every credit rating agency shall -***

(a)specify the rating process*;*

(b)file a copy of the same with the Board for record; and file with the Board any modifications or additions made therein from time to time.

(2) Every credit rating agency shall, in all cases, follow a proper rating process.

(3)Every credit rating agency ***shall have professional rating committees****, comprising members who are adequately qualified and knowledgeable to assign a rating.*

(4)All rating decisions, including the decisions regarding changes in rating, shall be taken by the rating committee.

(5) Every credit rating agency shall be staffed by analysts qualified to carry out a rating assignment.

(6)Every credit rating agency shall inform the Board about new rating instruments or symbols introduced by it.

(7) Every credit rating agency, shall, while rating a security, exercise due diligence in order to ensure that the rating given by the credit rating agency is fair and appropriate.

(8) A credit rating agency shall not rate securities issued by it.

(9) Rating definition, as well as the structure for a particular rating product, shall not be changed by a credit rating agency, without prior information to the Board.

(10) A credit rating agency shall disclose to the concerned stock exchange through press release and websites for general investors, the rating assigned to the securities of a client, after periodic review, including changes in rating, if any.

Board's right to inspect

29. (1) The Board may appoint one or more persons as inspecting officers, to undertake inspection or investigation of the books of account, records and documents of the credit rating agencies, for any of the purposes specified in sub- regulation(2)

(2).The purposes referred to in sub-regulation (1) shall be the following, namely:

(a) to ascertain whether the books of account, records and documents are being maintained properly;

(b)to ascertain whether the provisions of the Act and these regulations are being complied with;

(c)to investigate into complaints received from investors, clients or any other person on any matter having a bearing on activities of the credit rating agency;

(d)in the interest of the securities market or in the interest of investors.

*(3)***The inspections ordered by the Board under sub-regulation (1) shall not ordinarily go into an examination of the appropriateness of the assigned ratings the merits.**

(4)Inspections to judge the appropriateness of the ratings may be ordered by the Board, **only in case of complaints which are serious in nature.**

*(5)***Inspections referred to in sub-regulation (4) shall be carried out either by the officers of the Board or independent experts, with relevant experience or combination of both.**

THIRD SCHEDULE

2. A credit rating agency, in the conduct of its business, shall observe high standards of integrity, dignity and fairness in the conduct of its business.

3. A credit rating agency shall fulfill its obligations in a **prompt,** *ethical and* **professional manner**.

4. A credit rating agency shall at all times exercise due diligence, ensure proper care and exercise independent professional judgment in order to achieve and maintain objectivity and independence in the rating process.

5. A credit rating agency shall have a **reasonable** *and adequate basis for performing rating evaluations, with the support of* **appropriate** *and in depth rating researches. It shall also* **maintain records** *to support its decisions.*

……..

8. A credit rating agency shall keep track of all important changes relating to the client companies and shall develop **efficient and responsive systems** *to yield timely and accurate ratings. Further a credit rating agency shall also monitor closely* **all relevant factors that might affect** *the creditworthiness of the issuers."*

III. From the foregoing it will be seen that the expression of *opinion in standardised form*, i.e. a '*rating*', substantially depends on co-operation by the client {*Regulation 14(d)*} and it is when a client does not cooperate that the rating agency must have regard to the best available information in the public domain {*Regulation 16(2)*}.Therefore, at the very threshold the accusation that *'excessive*

reliance' was placed on information and co-operation provided by the client, is fundamentally misplaced.

IV. The overarching and overriding principle of commerce, also consistent with Indian constitutional principles is the presumption of *bona fides* and not the presumption *mala fides*. In other words, when two commercial persons engage, the standard expected of them under the Indian law is that they should presume *bona fides* unless, of course, there is evidence staring at them that the counterparty is acting *mala fide*. In the words of the Hon'ble Supreme Court, even a person placed in a fiduciary position, such as a director of a company, is not expected to convert himself into a suspecting detective distrusting every input received by him. Reliance is placed on *Chintalapati Srinivasa Raju v. SEBI, Civil Appeal No. 16805 of 2017, Supreme Court of India, Paras 17 and 21*. The above judgment cited with approval the ruling in *Dovey and the Metropolitan bank v. John Cory, [1901] AC 477.*The extract of the aforesaid order is as follows:

> *"17. There is no dispute that the appellant, who was wife of the Managing Director, was appointed as a Director of the Company— M/s Elite International (P) Ltd. on 1-7-2004 and had also executed a letter of guarantee on 19-1-2005. The cheques in question were issued during April 2008 to September 2008. So far as the dishonour of cheques is concerned, admittedly the cheques were not signed by the appellant. There is also no dispute that the appellant was not the Managing Director but only a non-executive Director of the Company. Non-executive Director is no doubt a custodian of the governance of the company but is not involved in the day-to-day affairs of the running of its business and only monitors the executive activity. To fasten vicarious liability under Section 141 of the Act on a person, at the material time that person shall have been at the helm of affairs of the company, one who actively looks after the day-to-day activities of the company and is particularly responsible for the conduct of its business. Simply because a person is a Director of a company, does not make him liable under the NI Act. Every person connected with the Company will not fall into the ambit of the provision. Time and again, it has been asserted by this Court that only those persons who were in charge of and responsible for the conduct of the business of the Company at the time of commission of an offence will be liable for criminal action. A Director, who was not in charge of and was not responsible for the conduct of the business of the Company at the relevant time, will not be liable for an offence under Section 141 of the NI Act. In National Small Industries Corpn. [National Small Industries Corpn. Ltd. v. Harmeet Singh Paintal, (2010) 3 SCC 330 : (2010) 1 SCC (Civ) 677 : (2010) 2 SCC (Cri) 1113] this Court observed: (SCC p. 336, paras 13-14)*
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> *"13. Section 141 is a penal provision creating vicarious liability, and which, as per settled law, must be strictly construed. It is therefore, not sufficient to make a bald cursory statement in a complaint that the Director (arrayed as an accused) is in charge of and responsible to the company for the conduct of the business*

of the company without anything more as to the role of the Director. But the complaint should spell out as to how and in what manner Respondent 1 was in charge of or was responsible to the accused Company for the conduct of its business. This is in consonance with strict interpretation of penal statutes, especially, where such statutes create vicarious liability.

14. A company may have a number of Directors and to make any or all the Directors as accused in a complaint merely on the basis of a statement that they are in charge of and responsible for the conduct of the business of the company without anything more is not a sufficient or adequate fulfilment of the requirements under Section 141."

Non-executive directors are, therefore, persons who are not involved in the day to day affairs of the running of the company and are not in charge of and not responsible for the conduct of the business of the company.

17.An instructive judgment of Lord Halsbury is contained in Dovey and the Metropolitan Bank v. John Cory [1901] AC 477. The Lord Chancellor put it thus:

"The charge of neglect appears to rest on the assertion that Mr. Cory, like the other directors, did not attend to any details of business not brought before them by the general manager or the chairman, and the argument raises a serious question as to the responsibility of all persons holding positions like that of directors, how far they are called upon to distrust and be on their guard against the possibility of fraud being committed by their subordinates of every degree. It is obvious if there is such a duty it must render anything like an intelligent devolution of labour impossible. Was Mr. Cory to turn himself into an auditor, a managing director, a chairman, and find out whether auditors, managing directors, and chairmen were all alike deceiving him? That the letters of the auditors were kept from him is clear. That he was assured that provision had been made for bad debts, and that he believed such assurances, is involved in the admission that he was guilty of no moral fraud; so that it comes to this, that he ought to have discovered a network of conspiracy and fraud by which he was surrounded, and found out that his own brother and the managing director (who have since been made criminally responsible for frauds connected with their respective offices) were inducing him to make representations as to the prospects of the concern and the dividends properly payable which have turned out to be improper and false. I cannot think that it can be expected of a director that he should be watching either the inferior officers of the bank or verifying the calculations of the auditors himself. The business of life could not go on if people could not trust those who are put into a position of trust for the express purpose of attending to details of management. If Mr. Cory was deceived by his own officers - and the theory of his being free from moral fraud assumes under the circumstances that he was - there appears to me to be no case against him at all. The provision made for bad debts, it is well said, was inadequate; but those who assured him that it was adequate were the very persons who were to attend to that part of the business; and so of the rest. If the state

and condition of the bank were what was represented, then no one will say that the sum paid in dividends was excessive.(at pages 485-86)

Per Lord Davey, it was held:

"In this state of the evidence, my Lords, I ask whether the course of business at the board meetings, as described by the respondent, was a reasonable course to be pursued by the respondent and other directors, or whether the knowledge which might have been derived from a careful and comparative examination of the weekly states and quarterly returns from the different branches of the bank ought to be imputed to the respondent, or (alternatively) whether he was guilty of such neglect of his duty as a director as would render him liable to damages. I do not think that it is made out that either of the two latter questions should be answered in the affirmative. I think the respondent was bound to give his attention to and exercise his judgment as a man of business on the matters which were brought before the board at the meetings which he attended, and it is not proved that he did not do so. But I think he was entitled to rely upon the judgment, information, and advice of the chairman and general manager, as to whose integrity, skill, and competence he had no reason for suspicion. I agree with what was said by Sir George Jessel in Hallmark's Case, and by Chitty J. in In re Denham & Co., that directors are not bound to examine entries in the company's books. It was the duty of the general manager and (possibly) of the chairman to go carefully through the returns from the branches, and to bring before the board any matter requiring their consideration; but the respondent was not, in my opinion, guilty of negligence in not examining them for himself, notwithstanding that they were laid on the table of the board for reference. The case is no doubt one of some difficulty, but the appellant has not made out to my satisfaction that the respondent wilfully (as that term is explained in the cases I have referred to) misappropriated the company's funds in payment of dividends." (at pages 492-493)

V. The term '*due diligence'* must follow the dictum of *'trust but verify'* and not the dictum of *'distrust and investigate'*. The SCN and its contents adopt the later approach.

B. RELIANCE ON CLIENT - REQUIREMENT OF LAW

I. The aforesaid principle squarely applies to a '*credit rating agency*' as well. The '*credit rating agency*', acting as a commercially prudent person, has been mandated by law to rely on co-operation from the client and in fact the client has been obligated by law to provide the CRA true, adequate and timely information {*Regulation 14(d)*}.

II. In the instant case, pursuant to Regulation 14(d), an agreement was indeed executed between ICRA and IL&FS to enable expression of opinion in a standardised form by ICRA on the creditworthiness of the instruments issued by IL&FS.

C. SALIENT FEATURES OF AGREEMENT WITH IL&FS

I. To further elaborate that '*rating'* is merely an opinion on the creditworthiness of the instrument and that reliance by ICRA on information by the issuer is part of the process of the rating, the relevant provisions of the rating agreement (*Annexure 8 to the Reply to the SCN, Pg. 78 at Pgs. 79-80 and 83-84*) are relied upon.

II. Particularly, the following has relied upon:

a. Disclaimer of advice and disclaimer of warranty at item *C (Pg. 80)*: The Clause (I) is in the nature of disclaimer by ICRA to IL&FS which states that the '*ratings'* provided by ICRA are not an audit opinion or any financial, legal, tax, advisory, consultative or business services and are not an advice on structuring, negotiating or drafting transactional documents. It provides that IL&FS must take independent advice on the abovementioned aspects.

b. Information to be provided by IL&FS at item (*Pg. 83*):

i. The Clause requires that information be provided by IL&FS to enable rating of instruments and their monitoring (*Clause I-V*).

ii. Particularly, IL&FS is to be provide details of non-cooperation with previous rating agencies (*Clause III*). Additionally, IL&FS is to provide information on delay/default in servicing debtobligations immediately, failing which, the same shall be considered to be suppression of material information and liable for action under SEBI Act and SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003.

iii. The format for the information to be provided on the instruments, at the time of signing of agreements is provided at *Clause V of Item I*, which also mandates provision of details of debenture trustees to enable ICRA to seek additional details from them.

c. Undertaking provided by IL&FS at item *J (Pg. 83):* This item provides that IL&FS would arrange for: information from other stakeholders such as auditors, bankers, management of IL&FS (*Clause I*); arrange for review of ratings on occurrence of material events (*Clause II*); provision of information to ICRA which will have impact on the '*ratings'*, including details of default or delay in payment of interest (*Clause III*); and provision of monthly no-default statement (*Clause V*).

d. Warranty by IL&FS on truthfulness and accuracy of information at item P (*Pg. 87*): As per item P, ICRA relies on information from IL&FS and from third parties provided on behalf of IL&FS, which ICRA will not be obliged to independently audit and verify. In this respect, IL&FS has provided warranty on the truthfulness and accuracy of the information and that such information is not misleading. Further, it provides that IL&FS has warranted that it has conducted reasonable due diligence in respect of such information.

III. Thus, there is a presumption of *bona fides* on an expert report and the information to be received by ICRA or '*credit rating agency*'.

D. PROTECTION AGAINST JUDGING APPROPRIATENESS

I. The next facet to be borne in mind from the foregoing provisions is that the CRA Regulations have taken care to stipulate that the judgment of a '*credit rating agency*' must not be called into question on the ground of appropriateness of the assigned rating {*Regulation 29(3)*}. It is only when complaints of a '*serious nature*' arise (the term *'serious nature'* is not defined) that an inspection may be ordered. Even for such inspection care has been taken to stipulate that the officers of SEBI or the independent experts, as the case maybe, who conduct such inspection must have relevant experience.

II. In fact, this is the reason why ICRA has repeatedly requested for a copy of the SEBI's file noting's. In view of Regulation 29, which is a carefully nuanced and balanced stipulation of inspection standard, it is ICRA's belief that the SEBI's file noting's thereon may contain counter balancing and mitigating findings or may have pointed out exculpatory facets of the matter. Such internal expressions of opinion made by persons mandated to have appropriate experience for such an exercise is a vital facet of evidence in play. It is once again requested that the same be provided to ICRA.

E. PROCESS RELEVANT NOT PRODUCT

I. Towards this end, i.e. protecting a '*credit rating agency*' from judgment of the appropriateness of its ratings, the CRA Regulations have also taken care to stipulate a regulatory focus on '*rating process*' and not '*rating outcomes*'. Regulation 24 sets out various regulatory requirements for conduct of '*rating process*'. There is not a whisper in the SCN that there was any violation of the '*rating process*'.

II. SCN's allegations imply that the '*credit rating agency*' '*rating*' is being judged for its appropriateness with the benefit of hindsight, in utter disregard of the protections stipulated in Regulation 29, despite the '*credit rating agency'* process having been fully compliant with Regulation 24.

III. Pursuant to the agreement with IL&FS, reliance is placed on each of the affirmations and confirmations (*Annexure 11, Pgs. 152 to 157*) provided by IL&FS pursuant to the Agreement under Regulation 14(d) (*Annexure 4 to Reply to SCN, Pgs. 52 to 64*). Specific reliance is placed on affirmation and confirmation provided by IL&FS dated August 1, 2018 (*Annexure 4 to Reply to SCN, Pg. 52 at Pg. 64*).

IV. When the performance of a '*credit rating agency*' is in fact to be judged in penal proceedings of this nature, the questions to be asked would be whether Regulations 14, 16 or 24 have been violated in its terms and not to ask whether the '*rating'* assigned was appropriate (which would violate the letter and spirit of Regulation 29). Reliance is placed on the rating rationale published to provide further colour to ICRA's expression of opinion in standardised form:

a. Rating Rationale dated March 27, 2018 (*Annexure 7 to Reply to SCN, Pgs. 70 to 77*);
b. Rating Rationale dated August 6, 2018 (*Annexure 6 to Reply to SCN, Pgs. 67 to 69*);
c. Rating Rationale dated September 8, 2018 (*Exhibit 1 to this Aide Memoire*); and
d. Rating Rationale dated September 17, 2018 (*Exhibit 2 to this Aide Memoire*).

V. It will therefore be seen that in fact ICRA reacted to information made available to it under Regulation 14, followed the procedures under Regulation 16 and applied the process set out in Regulation 24 and therefore, under Regulation 29, the '*appropriateness of the rating*' assigned must not be called into question. There is not a whisper of any facet of integrity of these compliances being compromised anywhere in the SCN.

VI. Regulation 24(7) requires a '*credit rating agency*' to exercise due diligence to ensure that the '*rating'* is '*fair'* and '*appropriate'*. Read harmoniously with Regulation 29 this would mean that one must have regard to the terms '*due diligence*' while expressing an opinion in standardised form without compromising the carefully nuanced protection accorded by Regulation 29. As stated above, the term '*due diligence'* does not connote adoption of a distrustful and suspecting attitude but must adopt an approach of a '*reasonable degree of verification*'. The rating rationale published by ICRA and referred to above clearly evidence that applying due diligence, ICRA indeed treated the inputs with a valid degree of scepticism and in fact reacted and altered its earlier opinions expressed. Such variations were dynamic in nature, responsive to a fair assessment and in fact demonstrated the reasonable conduct of rating process by ICRA.

VII. By referring to the provisions of the regulations and rating agreement between ICRA and IL&FS, it is submitted that while formulating a '*rating*', the reliance on information given by an issuer cannot be considered as excessive and that the law permits assumption of *bona fide* for information presented by the issuer.

VIII. Like in the case of a merchant banker, a '*credit rating agency*' role in a market is not that of an investigator, who is to proceed with distrust on the information provided by the issuer.

IX. From a plain reading of the Code of Conduct stipulated pursuant to Regulation 13, and extracted above it, would be seen that the SCN has nothing to show in terms of the '*ratings'* of ICRA not being '*fair'* or '*professional'* or '*non-independent'* for that matter. ICRA had reasonable and adequate basis for its evaluations and indeed has not only maintained records but has in fact provided SEBI with the same. The review and variation of '*ratings'* has been *bona fide*, prompt and responsive taking into account all relevant factors that could have affected the creditworthiness of the issuers.

F. EXCESSIVE RELIANCE - A VAGUE TERM

I. In view of the foregoing, it must be noted that an accusation of '*excessive reliance'* is not only contrary to the scheme of CRA Regulations but is also inherently vague, vitiating the SCN.

II. In fact, in spite of confirmation provided by IL&FS that there has been no default even as of August 1, 2018 (*Annexure 4 at Pg. 64*), ICRA had indeed downgraded the rating of NCDs issued by IL&FS on August 6, 2018. This alone will show that there was no '*excessive reliance'* on client confirmations. As shown on *Page 43* all relevant factors that may affect the creditworthiness of the issuer were noticed and discussed (*compliance with Clause 8 of Code of Conduct*).

III. The SCN has cherry picked statements from the said rationale to allege *'excessive reliance'* on certain factors and information provided by the issuer but it does not rely on other aspects that were considered along with disclosure of the risks to the credit profile.

IV. Ratings are neither an investment guarantee nor a recommendation to buy, hold or sell any securities (*Regulation 18*). They are an expression of opinion in a standardised form without precluding investor from doing his own '*due diligence'*. It was further emphasized that capital market is continuously evolving and new practices and steps are taken to make the market stronger, which is also the case with the rating of instruments. Thus, any adjudication of alleged

violations of the CRA Regulations is to be done on the basis of the process followed and material available to the '*credit rating agency*' at the relevant point in time and not in hindsight.

G. ON ALLEGATIONS IN THE SCN

I. The replies and submissions of the Noticee, *inter alia* are summarized as under: -

I. The inspection process is incomplete as SEBI has only provided part of the documents as requested vide an email dated August 9, 2019 and denied access to other documents sought by the Noticee vide an email dated August 19, 2019. The Noticee has still not been provided with copies of certain additional documents which it had sought vide its emails dated February 12, 2019 and March 1, 2019 pursuant to preliminary inspection on February 8, 2019. In this regard, the Noticee have issued letters dated April 3, 2019, May 2, 2019 and July 11, 2019, seeking such documents. As SEBI has denied access to certain documents vide an email dated August 19, 2019, which is a violation of the principles of natural justice, the Noticee reserves the rights to take appropriate action in this regard.

II. As a conscientious '*credit rating agency*', the Noticee has always been committed to its responsibilities to reflect its best professional assessment of the creditworthiness of the issuer of instruments rated by it. The opinions expressed reflected its *bona fide* position and most predictive view on the instruments it has rated. Where there was any change in the creditworthiness of the issuer whose instruments were being rated, it was reflected in its *bona fide* opinion on any such change, truthfully, transparently and promptly. Its opinions, as encapsulated in the rating rationales, disclosed the relevant factors which, both positively and negatively affected the credit profile of the issuer and the instruments issued. It would not be out of place to mention that varying views about the creditworthiness and future credit profile of an issuer of debt can be reached by different '*credit rating agencies*' on the same facts.

III. The Noticee in discharging its obligations and fulfilling its role in the market, it has followed the rating processes in compliance with CRA Regulations and relevant and applicable circulars as updated from time to time and its internal operations manual (collectively defined as "CRA Regime"). For over 27 years it has rated instruments of numerous types of issuers, including leading financial/investment institutions, manufacturing companies, commercial banks, non-banking finance companies, public sector undertakings and financial services companies.

IV. The Noticee approach in running its rating system seeks to balance publishing timely '*ratings'* that are predictive of an issuer's credit profile while avoiding precipitous '*ratings'* that are prone to significant reversals and lead to volatile and erratic '*ratings'*. The Noticee has always acted in a *bona*

fide manner and submits that it will provide full co-operation to the authorities on any query that is sought from it.

V. A CRA provides a third-party independent opinion of the '*creditworthiness'* of a particular issuer along with the '*creditworthiness'* of the instruments as are issued and being rated by the '*credit rating agency*'. An opinion by the '*credit rating agency*' refers to the relative ability and willingness of the obligor to meet its financial commitments, and soundness of the instrument i.e. the likelihood of the issuer to repay its debts, based on its own methodological approach in conjunction with the SEBI Act and CRA Regulations under the instrument being rated.

VI. The Noticee opinions on credit risk are amongst other things based on publicly filed information by the issuer and other publicly available information, including for example the audited financial results, and the review of any material updates and the public disclosures made by the issuers. It also augments this source of information with information *viz.* business and financing plans that it gathers through interactions with the issuer's management along with information attained from its interaction with them and their bankers, and statutory auditors. This results in the primary reliance being on publicly filed information of the issuer, as augmented by information from various sources including independent stakeholders such as market participants and other stakeholders (*including regulators, market infrastructures, investors, bankers, auditors, other CRAs, etc.*) which in absence of any contrary information or comments can be treated as accurate and consistent.

VII. The Noticee methodological approach, in undertaking any rating exercise, entails consideration of various factors for assigning a '*rating'* or suggesting a change to the same. Some of these factors represent credit strengths and other factors represent credit challenges. It is the job of the rating committees to exercise its best judgement, relying on amongst other things past experience, to apply these various factors to the available information, in the specific context of that point in time and consider likely outcomes. It asserts and confirm that it has followed this process in the case of instrument s issued by IL&FS and its entities.

VIII. The opinion of CRAs including the Noticee is based on various factors and cannot be attributed to/or categorized as a narration of future events. Merely because two viewpoints are possible, one cannot in hindsight render a view taken at a particular time to be vitiated in law or be considered as wrongful and *mala fide* in hindsight. The High Court of Bombay in the case of *SEBI vs Ikisan limited (2015) 6 AIR BOM R 291* also re-iterated an established principle that an exercise by an expert must be based on the date of the exercise - looking forward and cannot be reviewed in hindsight when there is no specific formula or mathematical calculation to be made.

IX. The capital markets work on the basis of disclosures made by an issuer whose securities are listed. Unlike statutory auditors or internal auditors, a '*credit rating agency*' has to necessarily work on the presumption of *bona fides* on the part of the issuer who makes the disclosures. The approach is one of the presumption of *bona fides* on the part of the issuer to its stakeholders, indeed tempered by a professional judgement from the '*credit rating agency*', but not with an approach of a questioning and judging the *bona fides* of every disclosure or approaching every piece of information with total suspicion and distrust. The CRA applies its processes and methodologies to the information disclosed by the issuer.

X. In formulating a '*credit rating*', the Noticee follows the following process, as required under Regulation 24(7) of the CRA Regulations, which is in line with its operating manual:

Step 1: Information and data gathering- This includes gathering of publicly available information disclosed by the instrument issuer, interactions with the bankers and statutory auditors of the issuer, monitoring of the websites of stock exchanges for listed issuers, monitoring of the repayment schedule and review of material events as specified under relevant SEBI circulars, and interaction s with issuer management.

Step 2: Analysis of information-Analysts analyses the information gathered from different sources and prepare a rating report recommending the appropriate rating action to the rating committee.

Step 3: Determination of the rating- The rating committee, which is comprised of senior analysts of various sectors, determines the appropriate rating action based upon the rating report and analyst recommendation.

Step 4: Assignment of the rating- The ratings, so determined, are communicated to the relevant issuer and thereafter a press release is published on ICRA's website that contains the rating rationale, key factors supporting the rating decision, rating methodology followed for determining the credit rating, along with the outlook/watch, if any.

Step 5: Ongoing monitoring- Once the credit rating has been published, ICRA monitor the credit rating on an ongoing basis, until it is withdrawn.

XI. In the case of IL&FS and IFIN, the Noticee followed the aforesaid procedure to gather information for analysis of its '*credit rating'*, which included review of the annual reports available in the public domain, and monitoring the debt servicing records through monthly no default statements. Additionally, in respect of the NCDs rated for IL&FS, ISIN-wise confirmation from

exchanges and/or debenture trustees was also reviewed. Moreover, it reviewed other information available in the public domain, feedback provided by IL&FS auditors and bankers, as well as the documents provided by and plans discussed with IL&FS in a series of meetings conducted with IL&FS's senior management and key managerial personnel.

XII. Based on the Noticee's ongoing analysis and monitoring of the information available, it began signaling the potential weakening credit profiles of IL&FS and its subsidiaries in its rating releases dated April 2017, November 2017, March 2018 and August 2018. Once it determined that the credit profile had indeed deteriorated, it acted and was one of the first voices in the market regarding the deterioration of IL&FS's credit profile by being the first '*credit rating agency*' to downgrade the '*rating'*.

H. Due Diligence

I. The Noticee was in compliance with applicable regulations and exercised proper due diligence, commensurate with its role as a '*credit rating agency*'. The Supreme Court of India has interpreted the meaning and scope of *'duediligence'* in the matter of *Chander Kanta Bansal v. Rajinder Singh Anand ((2008) 5 SCC 117)*, as follows:

> *"...according to Oxford Dictionary (Edn. 2006), the word "diligence" means careful and persistent application or effort. "Diligent " means careful and steady in application to one's work and duties, showing care and effort. As per Black's Law Dictionary {18th Edn), "Due Diligence" means the diligence reasonably expected from, and ordinarily exercised by, a person who seeks to satisfy a legal requirement or to discharge an obligation. According to Words and Phrases by Drain-Dyspnea (Permanent Edn. 13-A) "due diligence", in law, means doing everything reasonable, not everything possible "Due Diligence" means reasonable diligence; it means such diligence as a prudent man would exercise in the conduct of his own affairs..."*

II. Similarly, in relation to the role of a merchant banker, the term '*due diligence*' has come up for review time and again, both at the level of SEBI and indeed before the Hon'ble SAT. In its order *WTM/GM/EFD DRA-1/12/FEB/2017*, dated February 9, 2017, in the proceedings against *D&A Financial Services (P) Ltd* in the matter of *Brooks Laboratories Ltd.*, the Learned Whole Time Member of SEBI held that "*bearing in mind these principles governing 'due diligence', the merchant banker cannot be expected to look at each and every statement and information provided by the issuer with suspicion unless the facts and circumstances at the relevant time so demand. At the same time, the merchant banker is expected not to passively or mechanically disclose whatever is given to it by the issuer but to exercise reasonable diligence to ensure adequate, true and fair disclosures in the RHP/Prospectus."* The aforesaid ruling was also relied upon by the Adjudicating Officer appointed by SEBI in the matter of

Dr. Datsons Labs Ltd., (Formerly Anjaneya Lifecare Ltd.) (delivered on July 31, 2018), vide, the adjudication order No. *EAD-7/BJD/NJMR/107 /2018-19*.

III. Similarly, Hon'ble SAT in the case of *Imperial Corporate Finance and Services Pvt Ltd. v SEBI [2005] 61SC L197 (SAT)* has also agreed that *"...We however hold that before any person is found to have violated the concept of "due diligence", there must be an enquiry and the finding must be sustained by a higher degree of proof than that required in a civil suit, yet falling short of the proof required to sustain a conviction in a criminal prosecution. There must be convincing preponderance of evidence (see AIR 1984 SC 110)."* It is pertinent to mention that the Noticee is not an auditor (*much less a forensic auditor*) and does not/ought not to conduct '*due diligence*' consistent with the role of the audit industry.

IV. The Noticee formed a *bona fide* opinion on the credit worthiness of IL&FS and its subsidiaries, after thorough review and analysis of the relevant credit strengths and challenges. Its actions in analyzing the creditworthiness of IL&FS and its subsidiaries was reasonable and therefore, liability upon it cannot be imputed. As noted above, diligence in this context requires only doing what is reasonable but not everything possible. That is precisely what the Noticee has done. Hence, in the absence of positive evidence of '*actual malice*' in the assignment of the '*rating'*, or, at the least, gross disregard to stated and applicable methodology, it would be unfair to find fault with it. It must be remembered that '*ratings'* are not statements of facts but merely forward looking subjective *'opinions'* of a '*credit rating agency*' based on its analysis of the available information.

V. The allegation in the SCN is not that the Noticee acted with improper motivation or in a *mala fide* manner, but that it did not exercise its professional judgement and expertise in a prudent and diligent manner. In such a scenario, the burden of proof on SEBI is high to show that either irrelevant or improper factors were considered, or relevant factors were ignored, resulting in the rating opinion being arbitrary.

VI. The Noticee has applied its mind to the information provided by the Issuers and Management, including publicly available disclosures which IL&FS was legally obliged to make along with taking steps to corroborate the same through interaction with Management and feedback from bankers and auditors of IL&FS. This demonstrates that it had exercised proper professional judgment, in adherence with its operating process and rating methodology, and conducted reasonable diligence to ensure that the Management representations and financial information of IL&FS were reviewed and analyzed for the purpose of undertaking the rating actions with relevant publicly disclosed information and fair and appropriate '*ratings'* were assigned to the

instruments of IL&FS. There were no adverse feedback form lenders, auditors and debenture trustee. In light of the past track record of IL&FS and IFIN, there was no reason to expect future defaults by IL&FS and IFIN or extreme weakness in their respective financial position, that could have reasonably given it grounds to anticipate the sudden default by IL&FS as observed in September 2018. The Noticee's rating committees considered various factors that might be an area of concern in the future, and such factors were disclosed in its rating rationales. Therefore, it reiterates that it had exercised proper skill, care and diligence while assigning '*credit rating*' to the instruments issued by IL&FS and IFIN, and have responsibly discharged its duties as a '*credit rating agency*'.

I. <u>Hon'ble SAT judgment in the matter of Brickwork Ratings India Private Limited v. SEBI, Appeal No. 439 of 2018:</u>

"6. The AO has found that GPL had defaulted on NCDs due for redemption on December 1, 2014 in spite of which the appellant failed to downgrade the rating to "default" instead of downgrading the rating to "BWR BB-". It was also observed by the AO that the details of the default and restructuring were not mentioned in the Rating Rationale dated February 27, 2015. The AO further found that the mere fact that the said Company GPL subsequently rectified the default did not reduce the gravity of the violation and that the appellant was expected to act swiftly no sooner the default was made.

7. We find that the approach adopted by the AO is not correct. From a perusal of the minutes of the Central Rating Committee ('CRC') we find that the current outstanding balance of NCD of the Company and the Company being in dialogue with the investors for reschedulement was noticed and considered. A conscious decision was taken to downgrade the rating of the Company from "BWR A" to "BWR BB-". No Regulation or Circular has been shown to us by the respondent to indicate that whenever a default is made by a Company the CRA is required to automatically downgrade the Company to "default".

8. Regulation 24(7) of the CRA Regulations 1999 provides as under: -

> *"24.(1)…*
> *(2) Every credit rating agency shall, in all cases, follow a proper rating process.*
> *…*
> *(7) Every credit rating agency, shall, while rating a security, exercise due diligence in order to ensure that the rating given by the credit rating agency is fair and appropriate."*

9. The aforesaid provision indicates that a CRA is required to exercise due diligence in order to ensure that the rating given is fair and appropriate. In the instant case, we find that a conscious decision was taken by

the Central Rating Committee of the appellant and considering the default as well as the dialogue between the Company and with the investors with regard to reschedulement of the default the appellant recommended a revision of rating from "BWR A" to "BWR BB-". In our opinion due diligence was exercised. Thus, the order of the AO to this extent is not correct and cannot be sustained."

J. **Reply on Specific Allegations –**The SCN is broadly divided into four allegations and each of these is exhaustively dealt with in the Reply dated September 17, 2019. The following table is noteworthy:

Sr. No.	Allegation	SCN - Para & Pages	Reply - Para & Pages
1.	**Allegation of over-reliance/excessive reliance placed by ICRA on the information provided by the management of IL**&FS		
a.	Excessive reliance on the information provided by IL&FS with regard to updates of implementation of projects/deals/fund raising plans.	Para 5, Pg. 2	Para 26 to31, Pgs. 8-10
b.	Failure to track disclosures available and non-consideration of the divergence in information from the disclosures made to BSE.	Para 6-8, Pgs. 3 to 4	Para 32 to 38, Pgs. 10- ll
c.	Failure to conduct due diligence as high ratings accorded to the Non-convertible debentures ("NCDs") issued by IL&FS, despite declining financial indicators.	Para 9, Pg. 4	Para 39 to 42, Pgs. 12- 15
2.	**Allegation regarding failure to change rating outlook of the NCDs issued by IL&FS despite the slow pace of asset monetization**		
	Failure to change the ratings and revise the rating outlook from 'stable', on NCDs issued by IL&FS, prior to August 6, 2018, even though there was delay in divestment timelines.	Para 10- 11, Pgs. 4 to 5	Para 44-48, Pgs. 15 to 19
3.	**Allegation of failure to consider latest financials in the rating committee notes presented on October 27, 2017**		
a.	Failure to consider the financials as of June 30, 2017.	Para 12, Pg- 5	Para 49-50, Pg. 19
b.	Non-requisition of the asset liability mismatch statement as on June 30, 2017, with reliance on the statement as on March 31, 2017.	Para 13, Pg.6	Para 51-53, Pg. 20
4.	**Reliance by SEBI on observations of the Reserve Bank of India with regard to the rating done by ICRA of the commercial papers (CPs) of IL&FS and IL&FS Financial Services Limited ("IFIN") to allege lack of due diligence**		

a.	Undue comfort derived from the institutional parentage of IFIN, while failing to independently assess IFIN as a standalone entity and evaluate group risk aspects.	Para 14, Pgs. 6 to 8	Para 54-60, Pgs. 20 to 22
b.	Failure to downgrade the CP of IFIN from A1+, even upon occurrence of material events.	Para 14.V, Pg. 8	Para 61-63, Pgs. 22 to 23

13. I have considered the allegations levelled in the SCN, the reply/submissions of the Noticee and the relevant and relied upon material as available on record. Before dealing with the reply of the Noticee on merits, I deemed it appropriate to deal with technical objection raised by the Noticeewith regard to supply of documents relied upon in support of the allegations and the request of the Noticee with regard to inspection of several documents. It is noted from records that the allegations against the Noticee have been levelled on the basis of –

a) IL&FS disclosure to BSE dated July 21, 2018.
b) Copy of e-mail dated August 02, 2018 by IL&FS forwarded to the Noticee informing about the decision taken by its Board of Directors in meeting dated July 21, 2018.
c) Press Statement dated August 29, 2018 made by the IL&FS on website.
d) IL&FS disclosure to BSE dated August 29, 2018.
e) Rating Committee Notes of the Noticee dated March 30-31, 2016, March 31, 2017, October 27, 2017, March 23, 2018 and July 30, 2018 w.r.t. IL&FS.
f) Rating Rationales of the Noticee dated November 03, 2017, January 03, 2018 and March 27, 2018w.r.t. IL&FS.
g) Rating Outlook by ICRA for CPs issued by IL&FS dated March 27, 2018, August 06, 2018, September 08, 2018 and September 17, 2018 w.r.t. IL&FS.
h) IL&FS emails dated August 14, 2017 and September 20, 2017 to the Noticee forwarding details of ALM.
i) RBI letter dated November 22, 2018 to SEBI.

14. It is also noted that the copies of all the aforesaid documents have been provided to the Noticee during inspection of documents on February 08, 2019. Pursuant to the Noticee's e-mails dated February 12, 2019, March 01, 2019 and letters dated April 03, 2019, May 2, 2019 and July 11, 2019, the Enforcement Department of the SEBI provided the following documents to the Noticee vide e-mail dated August 09, 2019:-

a. Copy of letter dated November 14, 2018 issued by SEBI to RBI.
b. Copy of letter dated November 22, 2018 issued by RBI to SEBI in response to the above mentioned letter.

15. Vide e-mail dated August 19, 2019, the Enforcement Department of the SEBI declined the request of the Noticee for providing – (a) the copy of SEBI internal observations in the matter of credit rating by ICRA Limited and (b) copy of internal document of SEBI titled *'Format A - Annexure 7(2) - format for handing over fresh cases*', as copies of all the relied upon documents has been already provided to the Noticee in the matter. It is pertinent to mention that charge in this case is not based upon any formal inspection under Regulation 29 of the CRA Regulations rather the same is based upon examination of information and material available to SEBI, including the documents available in the public domain and the documents within the possession and knowledge of the Noticee itself. Further, the observations found during examination undertaken by SEBI that are the basis of allegation and charges are clearly spelt out in the SCN. Since that has been done and copies of all the relied upon documents had been provided to the Noticee to enable it to file its reply, in my view, the principle of natural justice has been duly complied with, in this case. Thus, in my view, no prejudice is caused to the Noticee, if SEBI has not provided it with copy of its internal note containing the observations of the examination undertaken in the matter. This view also finds support from the following judgment of Hon'ble SAT on the similar issue in the case of *Manoj Gaur Vs. SEBI, in Appeal Number* 64 of 2012 decided on October 03,2012: -

> *"The investigation report is not the evidence on which reliance was placed by the adjudicating officer. Since the adjudicating officer has complied with the statutory requirements, there is no legal obligation on the Board to furnish the entire investigation report to the appellants. Learned counsel for the parties have relied on certain case law relating to principles of natural justice. We do not consider it necessary to refer to all those details in view of the fact that regulation 9 of the Regulations makes it obligatory to communicate the findings in the investigation report and not the whole report. It is nobody's case that such findings were not made available. If the procedure laid down in the regulations has been followed by the adjudicating officer, the grievance of violation of principles of natural justice is without any foundation."*

16. The document mentioned at (b) above is neither relevant nor relied upon nor it can be of any use for the Noticee. In this context, it is pertinent to mention that while dealing with similar arguments as raised by the Noticee, Hon'ble SAT,vide its order dated May 12, 2017in *Satyam Computers case*, considered the order dated January 10, 2017 passed by Hon'ble Supreme Court in the matter of *Price Waterhouse* case and held and clarified that observations made by Hon'ble Supreme Court were general directions given as and by way of clarifications without going into the merits of the case and the same cannot be said to be the ratio laid down by Hon'ble Supreme Court applicable to all other cases. [*Para 21 page 40 of the order*]. It is also relevant to note that Hon'ble Supreme Court in the matter of *Kanwar Natwar Singh v. Directorate of Enforcement [(2010) 2 SCC 497],* has held that *"…Even the principles of natural*

justice do not require supply of documents upon which no reliance has been placed by the Authority to set the law into motion. Supply of relied on documents based on which the law has been set into motion would meet the requirements of principles of natural justice…" Further, in the matter of *Chandrama Tewari Vs. Union of India, Through General Manager, Eastern Railways, (1988) 1 SCR 1102,Hon'ble Supreme Court* has held that it is not necessary that each and every document must be supplied to the Noticee facing charges. Only material and relevant documents are necessary to be supplied to him. If a document, even though mentioned in the Memo of charges, is not relevant, or if it is not referred to or relied upon by the adjudicating officer or the punishing authority in holding the charges as proved against the Noticee, no exception can be taken to the validity of the proceedings on the ground of non-supply of the copy of such documents. As the Noticee has been given reasonable opportunities to file written representation and opportunity of personal hearing as per the Adjudication Rules, I am of the view that no prejudice has been caused to the Noticee, if documents not relied upon and internal examination observations were not provided to it.

17. In order to deal with the argument of the Noticee with regard to overview of the regulatory architecture for '*Credit Rating Agencies*', it is relevant to deal with the whole scheme of the SEBI Act and the measures taken by SEBI with regard to the role of the '*Credit Rating Agencies'* in pursuit of objectives enshrined in the SEBI Act. The SEBI Act, being a social welfare legislation to ensure an orderly growth of securities market and to protect the interest of the investors, has to be interpreted for furtherance of its purpose and not to frustrate it. Hon'ble Supreme Court in *SEBI Vs Ajay Agarwal* vide its judgment and order dated February 25, 2010 held as under: -

> *"39. If we look at the legislative intent for enacting the said Act, it transpires that the same was enacted to achieve the twin purposes of promoting orderly and healthy growth of securities market and for protecting the interest of the investors. The requirement of such an enactment was felt in view of substantial growth in the capital market by increasing participation of the investors. In fact such enactment was necessary in order to ensure the confidence of the investors in the capital market by giving them some protection.*
>
> *40. The said Act is pre-eminently a social welfare legislation seeking to protect the interests of common men who are small investors.*
>
> *41. It is a well -known canon of construction that when Court is called upon to interpret provisions of a social welfare legislation the paramount duty of the Court is to adopt such an interpretation as to further the purposes of law and if possible eschew the one which frustrates it.*

18. Further, a beneficial statute has to be construed in its correct perspective so as to fructify the legislative intent andprovision in the statute granting incentives for promoting growth and development should be construed liberally, so that real object of such enactment is not frustrated - *Bajaj Tempo Ltd.* v. *CIT AIR 1992 SC 1622.* Therefore, the interpretation of socio-economic legislation such as the SEBI Act and CRA Regulations, which are also aimed at social or economic development apart for investor protection, should not be narrow but should be in the perspective favouring the securities market and investors having regard to '*teleological purpose and protective intendment'* of the legislation.

19. Keeping the above principle in mind, in order to give purposeful meaning to the terms used in CRA Regulations, the scheme of the SEBI Act and '*measures'* taken thereunder need to be seen as a whole and not in fragmented manner. It is also deemed necessary look into the background of '*credit rating'* requirements necessitated by Regulators so as to understand the entire gamut and scope of responsibilities and accountability of '*Credit Rating Agencies'*. The preamble of the SEBI Act describes the object of SEBI (Board) i.e. to protect the interests of investors and to promote the development of and to regulate the securities market and for matters connected therewith or incidental thereto. Section 11(1) broadly prescribes the same objectives as duty of the Board established under Section 3 of the said Act and empowers the Board to take such *'measures'* as it thinks fit for carrying out those objectives and duties. It is relevant to mention here that, shortly after its establishment as statutory expert body, SEBI had issued "*Guidelines for Disclosures and Investor Protection"* vide its circular No. *PMD/Cir.4545/92 dated June 11, 1992 (Clause F)* and clarification thereto vide circular No. *PMD/Cir.4730/92 dated June 18, 1992. (Clause G).*These Guidelines / clarification had mandated the compulsory '*credit rating'* of debentures including NCDs where maturity exceeded 18 months. In addition, vide its circular No. *PMD/Cir. 9317/92 dated September 29, 1992*, SEBI issued *"Guidelines for to Developmental Financial Institutions for Disclosures and Investor Protection"* (Clause H) whereby it again mandated compulsory *'credit rating'* of debentures and bonds issued by companies/ corporations/institutions that are engaged mainly in developmental activities and which play a catalytic role in the industrial/infrastructural development of the country.

20. In pursuit of orderly development of debt/bond market the Central Government and respective sectoral regulators have, from time to time, taken several '*measures'*. Vide circular *F. NO.1/10/SE/94 dated July 20, 1994*, Government of India, Ministry of Finance laid down policy for listing of privately placed debt securities issued by companies and Financial Institutions in order to create a broader and more liquid market for privately placed debt securities issued by such companies/financial institutions. By this circular the Central Government exempted all categories of pure debt securities from the requirements of Rule 19 (2)(b) of the Securities Contracts (Regulation) Rules, 1957 (which applies for listing of securities on any recognized stock exchange) subject to the condition that such securities

shall carry a '*credit rating'* of not less than investment grade from any of the then existing '*credit rating agencies'* namely, *The Credit Rating Information Services of India, Ltd*.., *Investment Information and Credit Rating Agency of India Ltd.,* and *Credit Analysis and Research Ltd*. The list of such pure debt securities included NCDs, the non- convertible portion of partially convertible debentures (PCDs), deep discount bonds and commercial paper. It was further clarified that the privately placed debt securities already issued but not rated could also be listed on the stock exchange after obtaining the requisite '*credit rating'*. This policy was laid down with the view that the requirement of obtaining at least an investment grade '*credit rating'* for securities sought to be listed on the stock exchange would ensure protection of the interest of investors and the listing of privately placed securities on the stock exchange was expected to promote the development of an orderly and liquid secondary market for such debt securities.

21. The aforesaid requirement were subsequently consolidated in the SEBI (Disclosures and Investor Protection) Guidelines, 2000 and under Chapter X of the same, the '*credit rating'* of debt securities by a '*credit rating agencies*' continued as a measure for investor protection and for orderly development of the bond market. Apart from this SEBI also took several measures by issuing circulars with respect to issue, listing and trading of debt securities. For example, in order to provide the greater transparency in issuance and listing of privately placed corporate debt securities and to protect the interest of the investor, vide circulars no. *SEBI/MRD/SE/AT/36/2003/30/09 dated September 30, 2013* and *SEBI/MRD/SE/AT/46/2003 dated December 22, 2003*, SEBI had laid down certain requirements including the mandatory '*credit rating'* of not less than investment grade. Those requirements were applied with regard to already listed privately placed debt securities of the companies including PSUs as well. Consequent to these developments the Central Government had withdrawn its aforesaid circular dated July 20, 1994.

22. In view of growing importance of corporate bond market in national economy, SEBI had taken several steps based upon the*Report of High Level Expert Committee on Corporate Bonds and Securitization* of 2005. In order to facilitate development of a vibrant market for corporate bonds in India, the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 (ILDS Regulations) were notified. The ILDS Regulations, while provided certain relaxations, it emphasized adequate information disclosures, due diligence by involved intermediaries and more importantly '*credit rating*' as the cornerstones of transparency and investor protection. As per Regulation 4(2)(c) of the ILDS Regulations for public issue of debt securities the '*credit rating'* should be obtained from at least one '*credit rating agency*' registered with the Board and should be disclosed in the offer document. In terms of Regulation 20(b) of the ILDS Regulations for debt securities issued on private placement basis '*credit rating*' should be obtained from at least one '*credit rating agency*' registered with the Board. Further, Regulation 23 of the ILDS Regulations requires that - "*Every rating obtained by an issuer shall be periodically reviewed by the*

registered credit rating agency and any revision in the rating shall be promptly disclosed by the issuer to the stock exchange(s) where the debt securities are listed." Similar requirements were prescribed in the applicable listing agreements. Subsequently, by Regulation 55 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015 it was re-emphasised that - "*Each rating obtained by the listed entity with respect to non-convertible debt securities shall be reviewed at least once a year by a credit rating agency registered by the Board".*

23. Commercial Paper (CP) is an unsecured money market instrument issued in the form of a promissory note and regulated by the Reserve Bank of India (RBI). CP as a privately placed instrument, was introduced in India in 1990 with a view to enabling highly rated corporate borrowers to diversify their sources of short-term borrowings and to provide an additional instrument to investors. The RBI directives and guidelines issued from time to time under the Reserve Bank of India Act, 1934 also mandate '*credit rating'* for issuance of CP from either the Credit Rating Information Services of India Ltd. (CRISIL) or the Investment Information and Credit Rating Agency of India Ltd. (ICRA) or the Credit Analysis and Research Ltd. (CARE) or the FITCH Ratings India Pvt. Ltd. or such other credit rating agency (CRA) as may be specified by the RBI from time to time, for the purpose. The Insurance Regulatory and Development Authority, vide its IRDA (Investment) Regulations, 2000 has also mandated all insurers to make investments in specified securities graded by a reputed and independent '*credit rating agency*'.

24. It is also pertinent to mention that prior to 1995 the regulatory framework for registering and regulating the activities and conduct of '*credit rating agencies*' was missing. With effect from January 25, 1995section 11(2)(ba) of the SEBI Act was amended so as to include *registering and regulating* the working of '*credit rating agencies'* as one of the *'measures'* referred to in section 11(1). Section 12(1A) was inserted to provide a negative mandate for the *'credit rating agencies'* to act as such only in accordance with the conditions of a certificate of registration obtained from the Board in accordance with Regulations made by the Board. Though the provisions of section 12(1A) existed in the SEBI Act since 1995 there was no regulatory framework for regulation of the '*credit rating agencies'* till SEBI framed the CRA Regulations in 1999.It is also seen that the provisions of section 11(2) (ba) and section 12(1A) of the SEBI Act are co-terminus and must be interpreted to mean that the '*credit rating agencies*' that are registered and regulated by the Board under the CRA Regulations must also carry on their activities in furtherance of the aforesaid twin objectives of promoting orderly and healthy development of the securities market and for protecting the interest of the investors.

25. Regulation 2(1)(h) defines the expression *'credit rating agency'* as a "*body corporate which is engaged in,or proposes to be engaged in, the business of rating of securities offered by way of public or rights issue".* However, being

the beneficial legislations the SEBI Act as amended with effect from January 25, 1995 and CRA Regulations would apply with regard to debt securities issued and listed prior to coming into force of the said amendment to SEBI Act and commencement of the CRA Regulations and the '*credit rating agency* 'which has rated the debt securities of the issuers prior to the commencement of the CRA Regulations would be under obligations to comply with the provisions thereof including the code of conduct and all other prudential norms applicable to its '*rating'* activities whether the securities are issued to public or not. Further, as the '*rating'* obligations mandated under the aforesaid policies is a continuous obligation, the prescribed due diligence, independent assessment/ evaluation, monitoring of assigned '*ratings'* and creditworthiness of the issuers shall apply at all times till the obligation under the rated securities is outstanding or the issuer is wound up, whichever is earlier. Accordingly, SEBI can, at any time, look into the conduct of the '*credit rating agency'* so as to examine whether it has complied with its obligations or not. Any such examination, inspection or enforcement action cannot be construed as an action in hindsight as sought to be contended by the Noticee.

26. As regards the argument regarding the definition of '*rating',* it is pertinent to say that this word has to be understood in the context of the expressions '*credit rating agency*'. The term '*rating'* cannot be construed in isolation so as to limit it as any '*opinion*' regarding securities expressed in the form of '*standard symbols*'. When seen along with the real purport or role of a '*credit rating agency*', the term '*rating'* as defined in Regulation 2(1)(q) must be construed to apply for '*credit rating*'. *The* term '*credit rating'* has not been defined in the CRA Regulations but the word *'rating'* is defined in regulation 2(1)(q) of the CRA Regulations as "…. *an opinion regarding securities, expressed in the form of standard symbols or in any other standardised manner, assigned by a credit rating agency and used by the issuer of such securities, to comply with a requirement specified by these regulations;"*.It is gainsaying that SEBI has made aforesaid regulations and has taken '*measures'* which were meant to sub-serve the interest of investors as also promote and regulate the securities market. The CRA Regulations which are directly connected and concerned with the debt securities and financial instruments cannot be read in isolation and must be read and interpreted in the context in which they apply and operate i.e. the issuance, '*credit rating*' and listing of debt securities by companies/institutions/corporations. Further, considering the contemporary role and responsibilities of '*credit rating agencies'* in financial markets and the legitimate expectation towards creditworthiness of borrowers in a dynamic and constantly growing bond market, the content of the CRA Regulations must not be subjected to a narrow pedantic or lexicographic approach. Any attempt to truncate all-embracing scope and meaning of '*credit rating'*, would be to violate its widest possible amplitude and magnitude as enshrined in the SEBI Act, '*measures'* taken by SEBI for development of corporate debt market and investors protection. The '*credit rating'* is an ongoing and dynamic concept and it encompasses many aspects and dimensions and it cannot be cribbed, cabined and confined

within traditional and doctrinaire limits of the definition of '*rating'* with relation to merely an '*expression of opinion by symbols'* with a grammatical approach.

27. It is settled position that while interpreting social –economic welfare legislations, there should be more concern with the colour, the context and the content of the statute rather than its literal import. In this connection, I would like to make reference to the Judgment of the Hon'ble Supreme Court in *Reserve Bank of India vs. Peerless General Finance And Investment Co. Ltd. & Ors. - (1987) 1 SCC 424* wherein the Hon'ble Supreme Court at paragraph no. 33 has stated as to how statute should be construed after ascertaining legislative intent and in the context and scheme of the Act. Said paragraph no. 33 reads as under:

> *"33. Interpretation must depend on the text and the context. They are the bases of interpretation. One may well say if the text is the texture, context is what gives the colour. Neither can be ignored. Both are important. That interpretation is best which makes the textual interpretation match the contextual. A statute is best interpreted when we know why it was enacted. With this knowledge, the statute must be read, first as a whole and then section by section, clause by clause, phrase by phrase and word by word. If a statute is looked at, in the context of its enactment, with the glasses of the statute-maker, provided by such context, its scheme, the sections, clauses, phrases and words may take colour and appear different than when the statute is looked at without the glasses provided by the context. With these glasses we must look at the Act as a whole and discover what each section, each clause, each phrase and each word is meant and designed to say as to fit into the scheme of the entire Act. No part of a statute and no word of a statute can be construed in isolation. Statutes have to be construed so that every word has a place and everything is in its place. It is by looking at the definition as a whole in the setting of the entire Act and by reference to what preceded the enactment and the reasons for it that the court construed the expression 'Prize Chit' in Srinivasa and we find no reason to depart from the court's construction." (Also see JASBIR SINGH v. VIPIN KUMAR JAGGI & ORS. - (2001) 8 SCC 289).*

28. In *Bhavnagar University vs. Palitana Sugar Mill (P) Ltd. &Ors. - (2003) 2 SCC 111* in paragraphs 23, 24 & 25, Hon'ble Supreme Court observed thus:

> "*23. It is the basic principle of construction of statute that the same should be read as a whole, then chapter by chapter, section by section and words by words. Recourse to construction or interpretation of statute is necessary when there is ambiguity, obscurity, or inconsistency therein and not otherwise. An effort must be made to give effect to all parts of the statute and unless absolutely necessary, no part thereof shall be rendered surplusage or redundant.*

24. True meaning of a provision of law has to be determined on the basis of what it provides by its clear language, with due regard to the scheme of law.

25. Scope of the legislation on the intention of the legislature cannot be enlarged when the language of the provision is plain and unambiguous. In other words, statutory enactments must ordinarily be construed according to its plain meaning and no words shall be added, altered or modified unless it is plainly necessary to do so to prevent a provision from being unintelligible, absurd, unreasonable, unworkable or totally irreconcilable with the rest of the statute."

29. It is, thus, clear that the provisions of the CRA Regulations need to be looked at as a whole in setting of the entire Act and by reference to what preceded the enactment and the reasons for it and roles and responsibilities assumed by '*credit rating agencies'* in several measures taken by SEBI and other sectoral regulators. Further, in order to give purposeful meaning to any term the entire scheme of the SEBI Act and the CRA Regulations must be considered. In order to understand the scope of '*credit rating'* it is necessary to take into account the role of '*credit rating agency* 'in '*credit rating*' of a debt securities and any financial instruments. It is also pertinent to note that the relevant Regulations of CRA Regulations contemplate principle –based approach for conduct obligations of registered '*credit rating agencies'* so as to achieve regulatory objectives and for addressing new challenges and risks that may arise in the process of dynamic growth and development of the debt market. Further, considering the developments taken since the CRA Regulations came into the force before two decades and continuing an ongoing role and accountability of '*credit rating agencies'*, the definition of '*credit rating agency'* and '*rating'* should be interpreted adopting the dynamic theory and the meaning should be given with reference to the contemporary roles and responsibilities of the '*credit rating agencies'* so as to apply the CRA Regulations of 1999 in response to the changing needs and conditions as a '*living tree approach'*.

30. As accepted in common parlance a '*credit rating'* is an opinion of a '*credit rating agency*' as to the borrower's/ issuer's capacity to meet its financial obligations to the lender / investor on a particular issue or type of instrument in a timely manner. The '*credit rating*' measures the relative risk of the borrowers' / issuers' ability and willingness to repay both interest and principal over the period of the rated instrument. Thus, the '*credit rating*' signifies the creditworthiness of instruments and the issuer and also the 'probability of default' of the instrument that is rated. The limitation on this definition of '*rating'* as an '*expression of opinion*' of the '*credit rating agency'* regarding securities is that it cannot be construed as a recommendation to buy, hold or sell the securities (Regulation 18) nor it can predict default nor does it guarantee against loss. But it necessarily includes a qualitative well- informed and analysed opinion that largely influences the investment decisions.

31. The *'credit rating'* is effectively a pre-requisite for bond market access and also the minimum requirement for listing a corporate debt on the stock exchange. It has been well recognized and accepted position that '*credit rating'* quality has become the main criteria for investment in corporate bonds. In the contemporary situations, the '*credit rating agency*' play a crucial and important catalytic role in fostering the growth of the capital markets. A '*credit rating agency'* goes through thoroughly into all the relevant information before it announces its '*rating'* value. The '*credit rating'* is expected to encapsulate the analysis of the financials of the company, its strengths and weaknesses, its competitive position in the industry, and its future prospects. Thus, the '*credit rating agency'* accesses the financial strength of the borrowers/ issuers, specially their ability to pay the principal and interest on their debt. Therefore, '*terms'* and '*expressions'* used in the CRA Regulations must be interpreted in the context of the functional role in the contemporary situation instead of the mechanical and grammatical approach as sought to be contended by the Noticee. Further, the statutory requirements under the SEBI Act and CRA Regulations and obligation of the '*credit rating agency*' therein are reasonable restrictions on the fundamental rights under Article 19(1) (a) of the Constitution of India. The fundamental freedom of speech and expression of a '*credit rating agency'* while assigning a '*credit rating*' to any financial instrument is not absolute and is always subject to the statutory obligations under the SEBI Act and the CRA Regulations. Though the '*standard symbols*' assigned by a '*credit rating agency'* with regard to a security is not necessarily a statement of fact, it cannot be construed merely '*a symbol*' as sought to be argued. These '*standard symbols*' are of considerable significance as the investors in the corporate bond market rely largely on those '*rating symbols*' which are assigned by the professional '*credit rating agencies'* after a qualitative and independent evaluation of the creditworthiness of the instrument and the issuers thereof. Such '*rating symbols*' are considered as indicators of the creditworthiness as well the risk. A good '*credit rating'* can help the issuer to access high value investors both domestic and foreign. These symbols also serve as benchmark of financial market regulations.

32. In context of role and responsibilities of the '*credit rating agencies*' in securities market it is pertinent to refer to the following extracts from the "*Statement of The Technical Committee of The International Organization Of Securities Commissions"* dated 25 September 2003-

'"Credit rating agencies (CRAs, or ratings agencies) issue opinions on the future creditworthiness of a particular company, security or obligation as of a given date. These opinions tend to be relied upon by investors, lenders, and others, and, accordingly, CRAs can have an effect on securities markets in a variety of ways. Credit ratings can affect issuers' access to capital, influence the structure of financial transactions, and determine the types of investments fiduciaries and others can make. Some regulators use the ratings issued by CRAs for various regulatory purposes.

Given the influence CRA opinions can have on securities markets, the activities of CRAs are of interest to investors, lenders, issuers and securities regulators alike. The core objectives of securities regulation, as described by IOSCO's "Objectives and Principles of Securities Regulation," are protecting investors, ensuring that securities markets are fair, efficient, and transparent, and reducing systemic risk. In offering informed, independent analyses and opinions, CRAs contribute to achieving these objectives.

Rating agencies that the market recognizes as credible and reliable can play a valuable role in global securities markets…."

33. Going further in the scheme of the CRA Regulations it is noted that Chapter III provides for the general obligations of the '*credit rating agencies'*. Regulation 13 obligates the '*credit rating agency*' to abide by the code of conduct contained in the Third Schedule. Regulation 14 provides for an agreement between the '*credit rating agency*' and its clients and contents thereof. Regulation 14(d) obligates the client to cooperate with the '*credit rating agency*' and provide true, adequate and timely information. This regulation also envisages for the '*credit rating agency*' to arrive at, and maintain, "*a true and accurate rating*". Regulation 15 provides for the obligation of a '*credit rating agency*' to continuously monitor the rating of debt securities rated by it. The '*credit rating agency*' is further obligated to disseminate and disclose the information regarding newly assigned '*rating'* and changes in earlier '*ratings'* promptly. Regulation 16 provides for periodic review of all published '*ratings'* during the lifetime of the securities. It further provides that if a client does not cooperate with a '*credit rating agency*' in monitoring of the '*rating'* the '*credit rating agency*' must carry out the review on the basis of best available information or in the manner as specified by the board and disclose to the investor that '*rating'* is so based. Regulation 17 requires the '*credit rating agency*' to frame appropriate internal systems and procedures for monitoring the '*rating'* of securities by its employees. Regulation 18 obligates the '*credit rating agency*' to make the definition of the concerned '*rating'* public along with the '*symbol'* and also state that the '*rating'* do not constitute a recommendation to buy, hold or sell a security. Regulation 19 obligates to the '*credit rating agency*' to submit information to the Board. Regulation 20 requires it to comply with the circulars, guidelines, directives and instructions issued by the Board from time to time. Regulation 20A provides for appointment of a compliance officer who is responsible for the compliance of the securities law. Regulation 21 deals with maintenance of book, accounts and records *inter alia* with regard to rating assigned to various securities, rating notes of rating committee, record of decisions of rating committee and letter assigning '*rating'*, etc., Regulation 22 provides for obligation of '*credit rating agency*' to rectify the deficiency, if any, in the auditor's report and Regulation 23 provides for the confidentiality of the information between '*credit rating agency*' and its client.

34. It is very important to mention that Regulation 13 read with the Code of Conduct contained in Third Schedule of the CRA Regulations provide for the principle- based benchmark for the conduct of a '*credit rating agency*'. Some of the important benchmarks/ Code of Conduct in the said Third Schedule are as under:

a. Clause 1 requires a '*credit rating agency*' to make all efforts to protect the interest of investors.
b. Clause 2 of requires a '*credit rating agency*' to observe **high standards** of '*integrity'*, '*dignity'* and '*fairness'* in the conduct of its business.
c. Clause 3 obligates '*credit rating agency*' to fulfill its obligations, '*prompt'*, '*ethical*' and '*professional*' manner.
d. Clause 4 mandates that a '*credit rating agency*' shall ***at all times*** *exercise* ***due diligence****, ensure* ***proper care*** *and* ***exercise independent professional judgment*** *in order to achieve and maintain objectivity and independence in the rating process.*
e. Clause 5 provides that a '*credit rating agency*' shall have reasonable and adequate basis for performing **rating evaluations**, with support of appropriate and in depth rating researches.
f. Clause 6 mandates a '*credit rating agency*' to have in place a rating process that reflects **consistent and international rating standards.**
g. Clause 8 provides that a '*credit rating agency'* shall keep track of all important changes relating to the client companies and ***shall develop efficient and responsive systems to yield timely and accurate ratings***. Further a *'credit rating agency'* shall also ***monitor closely all relevant factors that might affect the creditworthiness of the issuers.***

35. Regulation 24 provides for the Rating Process and *inter alia* obligates the '*credit rating agency*' to follow a '*proper'* rating process, have professional rating committees and should be staffed by analysts to carry out a rating assignment. Regulation 24(7) provides a crucial obligation of a '*credit rating agency*' while '*rating'* a security. It commands the '*credit rating agency*' to "***exercise due-diligence in order to ensure that rating given by the CRA is fair and appropriate***".

36. The '*credit rating agency'* accesses the probability of default with respect to specific debt securities and the issuer. From the above regulatory scheme, it is noted that while the agreement with the client that specifies right and liabilities of each parties also *inter alia* requires the agreement on periodic review of the '*rating'*, co-operation of client in providing true, adequate and timely information to the '*credit rating agency*'. However, the obligation of the '*credit rating agency*' under Regulation 14(d) "*to arrive at and maintain* ***true and accurate rating*****"** cannot be diluted by any agreement as Regulation 16(2) clearly enables the '*credit rating agency*' to carry out the review of assigned '*rating'* on the basis of best available information or in the manner specified by the Board from time to time. Regulation 24(7) as it is

worded and intended requires the '*credit rating agency*' to give '*fair and accurate credit rating'* after exercising '*due diligence*'. Further, the aforesaid benchmarks/ conduct regulations in Regulation 16(2) read with Regulation 14(d), 13 read with Code of Conduct specified in Third Schedule particularly aforesaid Clauses 1, 2, 3, 4,5,6 and 8 and Regulation 24 (7) are not subservient to the agreement between a '*credit rating agency*' and its client. In the above scheme of the CRA Regulations the agreement between the '*credit rating agency*' and its client is a supplement to the aforesaid Code of Conduct and the regulatory requirements rather than to supplant them.

37. Thus, the regulatory scheme is clear that first and foremost obligation of a '*credit rating agency*' is to make all efforts to protect the interest of investors. As per the CRA Regulations, the '*credit rating agency*', at all times and in all circumstances, remains under obligation to give '*true'*, '*fair'*, '*appropriate*' and '*accurate*' rating and in order to fulfil such obligation the higher standards of due diligence, integrity, dignity, fairness, care, etc. are expected from it. The words '*true'*, '*accurate', 'fair'* and '*appropriate*' with regard to obligation for giving rating are of much significance and they expect higher degree of skill, care and diligence from the '*credit rating agency*'. Thus, the '*credit rating agency*' is not merely to accept mechanically the information given by its client but is also required to have an independent professional judgment about the quality of information, creditworthiness of the client and about the probability of default of the respective debt security based on any other available information. The obligations to exercise independent professional judgment in order to achieve the objectivity and independence in the rating process requirements requiring reasonable and adequate basis for performing rating evaluations with the support of appropriate and in depth rating researches coupled with ability to use available information and the obligation of exercising due diligence, proper care and ethics, clearly negate the argument of the Noticee that discharge of its obligation is substantially dependent on the cooperation of the client and that the issuer is solely responsible for the quality of information. The presumption of *bona fide* would help if the compliance with the desired Code of Conduct is shown. The above scheme of the CRA Regulations does not require existence of *mala fide* or bad motive in order to bring home the charge. Once it is established that a '*credit rating agency*' has failed to comply with its statutory obligations under the CRA Regulations the consequences would follow. In view of these findings, I hold that the judgment in the case of *Chintalapati Srinivas Raju* is of no help to the Noticee.

38. In my view, the '*credit rating agency*' is expected to provide an independent evaluation of the creditworthiness of the debt securities issued by the issuers. The independent, comprehensive and objective analysis and judgment about the debt instrument and subsequent and impartial assessment and judgment of default risk by a professional '*credit rating agency'* offer several benefits to the economy, bond market, the borrower and the investors both domestic and foreign. Any other interpretation as

sought to be contended would render the CRA Regulations unintelligible, unreasonable, unworkable and irreconcilable with the object of the SEBI Act and the CRA Regulations.

39. The Noticee has submitted that the *due diligence* must follow the dictum of '*trust but verify'* and not the dictum of *'distrust and investigate'*. Further, like in the case of a merchant banker, a '*credit rating agency*'s' role in a market is not that of an investigator, who is to proceed with distrust on the information provided by the issuer.It is also settled position that *'due diligence'* means careful and persistent application or effort. It requires careful and steady in application to one's work and duties, showing care and effort [*Chander Kanta Bansal Vs. Rajinder Singh Anand [(2008) 5 SCC 117*]. Normally, the degree of prudence in this regard is the diligence reasonably expected from, and ordinarily exercised by, a person who seeks to satisfy a legal requirement or to discharge an obligation. It means such diligence as a prudent man would exercise in the conduct of his own affairs. With regard to such obligations of '*credit rating agency*', it is relevant to mention that a '*credit rating agency*' plays a crucial and pivotal role not only to further its or its client's interests but also to protect the investors and securities market at large. Often, it has been observed that this duty to exercise due care and diligence has come in conflict with the pecuniary interests of the intermediary. It is seen that it has been a consistent stand of the Hon'ble SAT to seek a balance while dealing with such conflicting interests, with a justifiable tilt in favour of the larger interest of the securities market. In *JM Mutual Fund and JM Capital Management Private Limited Vs. SEBI* [SAT order dated 22.11.2004] Hon'ble SAT held that -

> *"40. In our view no hard and fast rule or straightjacket method can be applied with regard to the principles of due diligence. Due diligence is nothing but a watchful caution and foresight as the circumstances of the particular case demands. (see P-Ramanathan Aiyar's Law Lexicon 1997 edition page 599)*
>
> *41. The due diligence is an obligation to exercise reasonable care. Black's Law Dictionary, 6th edition defines "Due Diligence" at page 457as follows:*
>
> *"Such a measure of prudence, activity or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent man under the particular circumstances; not measured by any absolute standard, but depending on the relative facts of the special case."*

40. Thus, the obligation of *'due diligence'* varies according to a given situation and the same cannot have hard and fast rule or straightjacket method or absolute standards or any single sacrosanct nature for determination of '*due diligence'*.

41. The Noticee has forcefully contended in its reply that in terms of provisions of Regulation 14(d) it is the obligations of issuer to cooperate with the 'credit rating agency' to enable it to formulate its rating.

The allegation of 'excessive reliance' is not only contrary to the scheme of the CRA Regulations but also is inherently vague. The submissions of the Noticee in this regard though attractive in the first blush but the closer scrutiny of the overall scheme of the CRA Regulations as above would show otherwise. In terms of *Regulation* 14(d), the obligation is to write an agreement between the '*credit rating agency*' and its client whereby the client is under the obligation to cooperate with '*credit rating agency*' and to provide it true, adequate and timely information. Under this Regulation, the reasonable and legitimate obligation of the '*credit rating agency*' remains that it has to arrive at and maintain, a '*true'* and '*accurate'* rating. Under the CRA Regulations, the '*due diligence'* expected from a '*credit rating agency*' is much more than just to '*trust but verify'* the information received from the client. Such obligations is much more than that. The high standards of the conduct obligations under the aforementioned clauses of Third Schedule entail that the '*credit rating agency*' must exercise independent professional judgment at all times in order to achieve and maintain objectivity and independence in rating process. The '*objectivity'* and '*independence'* is very important and crucial element in the '*due diligence'* to be exercised by the '*credit rating agency*'. This apart, the specific and very important obligation of the '*credit rating agency*' to have in place the rating process that reflects consistent and international rating standards further expects higher and special degree of '*due diligence'* from a '*credit rating agency*'. Such '*due diligence'* would follow that the '*credit rating agency*' should receive the information from the client, independently verify and confirm the '*truthfulness'*, '*adequacy'* and '*promptitude'* of the same for the purpose of arriving at and maintaining '*a true and accurate rating'* of the securities of the client {*Regulation 14(d)*}and if, the client does not cooperate in provide the true and adequate information, then use the best available information {*Regulation 16(2)*}and exercise independent professional judgment with the support of appropriate and in depth rating researches and using rating processes that reflect consistent and international rating standards{*Regulation 13 read with Third Schedule and Regulation 24(7)*}. It is in the context of determining such legitimately expected '*due diligence'* that the expression *'excessive reliance'* has been used in the SCN. What it actually contemplates and envisages is that - the Noticee failed to exercise independent professional judgement in order to '*achieve and maintain' objectivity and independence in the rating process.* In my view, while applying the CRA Regulations, which have *bona fide* purpose of investors' protection and orderly development of securities market, the object of the Regulations should not be pushed aside giving way to mere technicalities and any measure in the interest of the investors which would pass the legal tests provided in the Regulation should be welcome. It is obligatory upon the Regulator to apply the law keeping in mind the objective and purpose of the Regulations and it must evince rational interpretation and not be influenced by moral propensity.

42. The *due diligence* expected form a merchant baker has to been seen in the context of the activities of a merchant banker. A merchant banker, while discharging its activities as such in the issue process or other specified activities, is obligated to exercise independent professional judgment and owes a crucial

responsibility towards protection of interests of investors and not merely to further its commercial purpose for pecuniary benefits. Thus, its role is also not limited to just receive information from issuers or its management and simply 'trust and verify' without applying its independent professional judgement. In the case of *'credit rating agencies'*, the '*due diligence'* obligations in Third Schedule of the CRA Regulations are much wider than the '*due diligence'* obligations of a merchant banker under the SEBI (Merchant Bankers) Regulations, 1992 as discussed hereinabove. Further, in view of the scheme and object of the CRA Regulations as discussed hereinabove, the *due diligence* obligation of a '*credit rating agency*' is a continuing obligation and it has to ensure compliance with the same at all times. The power of SEBI to examine such compliance obligations is not limited to look only prospectively. If it is observed that the '*credit rating agency*' has failed in exercise of its obligations in the past SEBI can look into the same for the appropriate action in the interest of the investors and securities market. Therefore, it is not correct to say that the instant adjudication of alleged violations of the CRA Regulations is in hindsight as sought to be contended by the Noticee. It is well settled in the above mentioned *Ajay Agrawal* judgment that action can be taken by the Board for past defaults if on the date of order the power to pass order exist. I, therefore, do not agree with submissions of the Noticee in these regards.

43. Another submission of the Noticee is that in terms of Regulation 29(3) of the CRA Regulations the judgment of a '*credit rating agency*' must not be called into question on the ground of *appropriateness of the assigned rating.* It is only when complaints of a '*serious nature*' arise that an inspection may be ordered. Even for such inspection care has been taken to stipulate that the officers of SEBI or the independent experts, as the case may be, who conduct such inspection must have relevant experience. At the first place as seen from the SCN, SEBI has not sought to examine the *appropriateness of the assigned rating* on merits. In this case, SEBI has examined whether the Noticee has exercised *due diligence* in the rating of the NCDs of IL&FS. The charge is for inquiry and adjudication as to whether the Noticee has failed to observe the obligations under Regulation 24 (7) and Clause 4 and 8 of Code of Conduct read with Regulation 13 of the CRA Regulations in the facts and circumstances as observed during the examination by SEBI. I Further, such embargo, if any, is applicable only during inspection of the '*credit rating agency*'. In this case SEBI has not ordered any inspection and Regulation 29 does not apply accordingly in this case. The instant proceedings have been initiated under Chapter VIA of the SEBI Act based upon the examination of information as mentioned hereinabove. The power to initiate inquiry and adjudication is not necessarily to be preceded by an inspection under Regulation 29. Under the plenary power in the SEBI Act, it is the choice and discretion of the Board to take any appropriate enforcement action at any stage, if it is *prima facie* satisfied that the '*credit rating agency*' has contravened any of the provisions of the CRA Regulations. Once it is *prima facie* found that '*credit rating agency*' has failed to comply with the conduct regulations as mentioned above it need not order inspection and

right away initiate appropriate enforcement action. I, therefore, do not find merit in these submissions of the Noticee.

44. It is also pertinent to mention that the events that occurred in the year 2009 in the global financial system had underlined the pivotal role that *credit ratings* play in debt markets. In the wake of the same and in order to impart higher credibility to the processes and procedures associated with the *credit rating,* SEBI, vide Circular Number CIR/MIRSD/CRA/6/2010 dated May 03, 2010 specified several transparency and disclosure norms for *'credit rating agencies'*. Those prescriptions included detail requirements with regard to '*rating process'*, *' rating procedures'* '*default studies'* and '*disclosures'*. It emphasised that default studies are central to evaluating the performance of a '*credit rating agency'* and whether its ratings can predict default over a period of time. In order to promote transparency and to enable the market to best judge the performance of the ratings, the '*credit rating agencies'* were directed to publish information about the historical default rates of rating categories and whether the default rates of these categories have changed over time, so that the public can understand the historical performance of each category and if and how rating categories have changed, and be able to draw quality comparisons among ratings given by different *credit rating agencies'*. Thus, it is clear that the standards of compliance obligation of *credit rating agencies'* in Third Schedule read with regulation 13 and Regulation 24(7) are much higher than those for any other intermediary.

45. When seen in the context of CRA Regulations as discussed above, the *credit rating agencies'* are also under a very important obligation to to have in place a rating process that reflects consistent and international rating standards. By aforesaid circular dated May 03, 2010 it was also obligated that the *credit rating agencies'* should disclose the compliance status of each provision of IOSCO code of conduct. These requirements are though not charged as violation in this case, they are relevant for determining the overall *due diligence* obligations of the Noticee in the facts and circumstances of the instant case. It is noted that The *'IOSCO CRA Principles' inter alia* address following key objectives to promote informed, independent analyses and opinions by *credit rating agencies'* :

- **Quality and integrity of the rating process**: *credit rating agencies* should endeavour to issue opinions that help reduce the asymmetry of information among borrowers, lenders and other market participants.

- **Transparency and timeliness of ratings disclosure**: *credit rating agencies'* should make disclosure and transparency an objective in their ratings activities.

46. The international standards adopted by '*credit rating agencies'* include the 'distance to default' and the 'probability of default' as the essential credit risks in the financial markets. Such assessment of credit

risks provides an estimate of the likelihood that an issuer will be unable to meet its debt obligations. It is crucial for the '*credit rating agencies'* to know which parameter effects more on 'distance to default' and the 'probability of default' so that investors will prevent future risks.

47. In my view , if the interpretation on the basis of prescriptive approach as forwarded on behalf of the Noticee is adopted it will lead to make application of regulatory scheme too constrictive and will defeat the object and purpose of the SEBI Act and the CRA Regulations. I also hold the view that such an interpretation will create hindrance in achieving regulatory objectives and would enable the '*credit rating agencies'* to be lax in their important statutory obligations.

48. Having dealt with all technical submissions and those on regulatory overview and architecture and now coming to the merit of the case to determine as to whether the Noticee had duly complied with Regulation 24(7) and Clauses 4 and 8 of Code of Conduct for the '*credit rating agencies*' read with Regulation 13 of the CRA Regulations, it is noted that the allegations in this case are levelled in the background of default committed by IL&FS and its subsidiary IFIN on their obligations in respect of the CP, ICD and also default on interest payments on its NCDs and the role of the Noticee in assigning rating to various NCDs of IL&FS. It was observed that IL&FS had defaulted on its obligations in respect of the CP issue and ICDs which was due on September 14, 2018. The said CP was rated by the Noticee, among other CRAs. Subsequently, IL&FS also defaulted on the interest payments on its NCDs on September 17, 21, 26 and 29, 2018. Further, the Noticee had downgraded the ratings of the NCDs issued by IL&FS on various occasions as described in the SCN.

49. The Noticee has claimed that it was continuously monitoring the IL&FS and its group companies, was meeting with management/ auditors/ bank officials related to IL&FS and gathering information available in public domain and was well aware of the plan of raising capital by IL&FS through various mode including the said right issue of ₹4,500 crore. It is established fact that the decision of IL&FS with regard to equity infusion by way of rights issue amounting to ₹4,500 cores taken on July 21, 2018 was informed to the Noticee by IL&FS but the said material information was not disclosed to the stock exchange by it. It is matter of common prudence that whenever a listed entity comes with a right issue it has to promptly disclose the same to the stock exchanges. When the Noticee was informed by IL&FS about the approval of the said right issue by IL&FS, it has not put any effort to verify the same from the stock exchange. When IL&FS made the claim about its said right issue and *Specific Asset Disinvestment plan* to reduce its overall debt by ₹30,000 crores on August 29, 2018 *via* a disclosure on its web site and informed the Noticee about the same, the Noticee again did not verify the truth and veracity from the disclosures made on stock exchange. As a reliable 'credit *rating agency'* it would be prudent to verify the information received from the publicly disclosed information. I also note that the disparity in the disclosures made by IL&FS in its Press Statement and the information submitted

to BSE in this case had resulted in information asymmetry, and that should have triggered a '*red flag*' to the Noticee, being a registered '*credit rating agency'* for rating the IL&FS and its debt instruments. In my view the Noticee lacked in exercising reasonable prudence of responsible *credit rating agency* and was lagging in exercise of desired due diligence.

50. In terms of slow progress of some of the projects highlighted in the SCN *viz*., ITCPL Cuddalore Thermal Power Plant, Yu He Expressway and IL&FS Securities Services limited the Noticee has provided following explanation:

a. **ITCPL Cuddalore Thermal Power Plant:** The Noticee acknowledged the slow progress in the signing of PPA of the Unit-11 of the project in its rating reports for October 27, 2017 and March 23, 2018. It had noted that ITPCL had started selling merchant power on spot basis, while the PPA for its second unit of Cuddalore project was pending. Thereby, the project was expected to be self-sufficient with no funding requirement for meeting cost or debt obligations.

b. **Yu He Expressway:** Based on the Noticee discussions with the Management held on March 21, 2016, as included in the rating report dated March 30-31, 2016, Management was in contemplation of partial divestment of Yu He Expressway. As per management and publicly available information, discussions for such divestments and monetisation plans were at advanced stages for a few of the SPVs. During its meeting with Management on March 03, 2017, it was informed that the management of ITNL was further considering other activities, including launch of lnviTs (for which roadshows were underway), public issue and divestment plans for certain of its assets in that fiscal, while the discussion on divestment of its stake in Yu He Expressway was still underway.

The same was adequately captured in its rating report dated March 31, 2017. Thereafter, in its report dated March 23, 2018, the Noticee had noted that a term sheet for divestment of the expressway was in place and the project has received the approval for tolling an additional stretch, because of which, the valuation was expected to be higher.

c. **IL&FS Securities Services limited:** The Noticee acknowledged that the progress had been slow due to the regulatory approvals required for closing the transaction. Since both ISSL and lnduslnd Bank were regulated entities, multiple approvals from different regulators were required, which was a time consuming process, post which the entities would seek approval from SEBI and stock exchanges. The rating report dated March 23, 2018 further noted that Management expected RBI approval for the sale of ISSL to lnduslnd Bank in the near term.

51. The Noticee further submitted that despite the slow progress in the divestment schemes and other asset monetisation plans by IL&FS, it had been regularly monitoring the updates on Management's plans contained in publicly available documents, and had reasonable grounds to believe that the I&FS Group would be able to achieve the divestments and asset monetization plans under consideration given the Group's past experience and track -record in terms of monitoring projects. Accordingly, it did not change the outlook to '*Negative'* but adequately highlighted the same in the reports and rationales. In this regard, I note that the slow progress in the divestment schemes and other asset monetization plans by IL&FS had affected its revenue generation and subsequently IL&FS and its group companies failed in meeting their debt obligations and defaulted in payment of NCDs and interest payments. It is undisputed fact that the Noticee had maintained the Rating Outlook on the NCDs of IL&FS as "Stable" throughout the rating period despite the slow pace at which the asset monetization and deleveraging steps of IL&FS was taking place. In the rating rationales given by the Noticee on January 03, 2018 and March 27, 2018 it had given the outlook as 'stable' despite stating that the outlook might turn negative if, *inter alia*, there is significant deviation in the execution of divestment plans which would impact its deleveraging plans.

52. From the rating committee notes dated March 31, 2016, March 31, 2017, October 27, 2017 and March 23, 2018 it is noted that IL&FS had provided the timeline for monetisation of its various projects. From the perusal of the aforesaid plan submitted by IL&FS to the Noticee, it is observed that some projects like signing Power Purchase Agreement (PPA) by Unit II of Cuddalore Power Plant, sale of YuHe Expressway, IL&FS Securities Services were in pipeline since March 2016 and there was no sign of completion of these projects even in March 2018. Further, the plan of launching InvITs by IL&FS, which was communicated by the IL&FS to Noticee in March 2017, was also put on hold for one year. Thus, it is clear that the Noticee despite being aware of the aforementioned facts indicating inordinate delays in monetisation of assets by IL&FS/ generating cash flows, maintained the outlook for the debt instruments of IL&FS as stable. The Noticee failed to adequately caution the investors regarding the high leverage and delay in implementation of asset monetization plans by IL&FS as it was waiting for further deviations to turn the outlook to negative.

53. It is also admitted fact that the ratings were placed under "*Watch with developing implications*" only in August 06, 2018, while downgrading the rating to AA+. It is also admitted fact and a matter of record that the borrowings of IL&FS had increased from Rs. 12,122.20 crore on March 31, 2017 to Rs. 13,113.10 crore as on June 30, 2017. However, these figures were not presented by the Noticee to its rating committee in the note presented on October 27, 2017 and were also not disclosed in the Rating Rationale dated November 3, 2017. It is also undisputed fact that figures for ALM as on March 31, 2017 was considered by the rating committee of the Noticee in its meeting dated October 27, 2017

instead of considering the ALM figure as on June 30, 2017. In fact the Noticee did not make an effort to sake ALM figure as on June 30, 2017 from IL&FS when it provided on September 20, 2017 the ALM figures as on March 31, 2017. Considering the fact that ALM figure as on June 30, 2017 would have been the most important point of analysis as the business of NBFCs/ CICs depends on their ability to maintain a comfortable asset – liability position across various buckets, such conduct shows glaring lack of prudence and due diligence.

54. The sum and substance of the explanation of the Noticee on the specific allegations is that it had consistently considered the reliance on the information from the management and the board of the issuer as prudent. It has analysed the information gathered from different sources and prepared the rating report. The Rating Committee determines the appropriateness of the rating based on the rating report and analyst recommendation. It adopts rating methodology for determine the rating alongwith outlook/ watch, if any. Based on its ongoing analysis and monitoring of the available information it has started signalling the potential weakening credit profile of IL&FS and its subsidiaries in its several rating releases from April, 2017. Once it determined that the credit profile of IL&FS had indeed deteriorated it acted promptly being the first '*credit rating agency'* to downgrade the ratings despite No Default Statement letter dated August 01, 2018 from IL&FS.

55. It is relevant to mention that the important financial parameters, as noted from the standalone and consolidated balance sheet of the IL&FS (Source: IL&FS website) during Financial Years ending on March 31, 2015, March 31, 2016, March 31, 2017 and March 31, 2018 show as following:

All figures in ₹ Million

S.No.	Particular	March 31, 2015	March 31, 2016	March 31, 2017	March 31, 2018
Standalone (IL&FS)					
1	Long Term Borrowings	83723	96056	93440	101790
2	Current Maturities of Long Term Debt	7029	12933	14709	23848
3	Short Term Borrowings	11049	19913	13072	33714
4	Proceeds from Sale in Investments in Subsidiaries/ Associates	27980	13958	7010	2136
5	Revenue	14303	19124	17872	18994
6	Operating Profit	3261	3992	3596	3324
Consolidated (IL&FS)					
1	Long Term Borrowings	486486	546651	597640	652935
2	Current Maturities of Long Term Debt	77187	64443	97449	122386
3	Short Term Borrowings	67466	92649	122386	105087
4	Proceeds from Sale in Investments in Subsidiaries/ Associates	2654	9855	7518	1046
5	Proceeds from sale of Other Non-current Investments	2084	2843	9897	1508
6	Proceeds from Sale in Investments in Associates	0	0	3926	379

7	Operating Profit	7043	5208	6177	-21092
8	Revenue	116405	150977	171564	187986
9	Expenses	109361	145769	165388	209080
10	Borrowing Cost	45175	54979	65165	79228
11	Cost of Raw Materials	5527	6854	14641	22167

56. From the above table it is observed that:-

a. The expenses of the IL&FS on consolidated basis was increasing continuously i.e. 33% in FY 2015-16, 13% during FY 2016-17 and 26% during FY 2017-18. Two of the main contributing factors in the rise in expenses of IL&FS as a group are – Borrowing Cost and Cost of raw materials, apart from Operating and Administrative Expenses and Sub Contracted Construction Cost and others. The increase in revenue during the same period for IL&FS on consolidated basis was also increasing continuously i.e. 29% in FY 2015-16, 13% during FY 2016-17 and 9% during FY 2017-18. On comparison of both it is seen that increase Revenue and Expenses were in tandem till FY 2016-17, however, the situation in FY 2017-18 was different, wherein rise in expense was almost three times that of revenue, contributed by rise in borrowing cost and cost of raw materials.

b. The operating profitability of IL&FS on standalone as well as consolidated basis was subdued, especially when the same is compared with the increase in its revenue from operation. It is noted that on consolidated basis, during FY ending on March 31, 2016, there was fall in operating profit of approx. 26%. Similarly, on standalone basis, during FY ending on March 31, 2017, there was fall in operating profit of approx. 10%. This shows that IL&FS was facing issues to maintain its business profitability.

c. The cash flow from the proceeds from sale in investments in Subsidiaries or Associates of IL&FS on consolidated basis was declining during FY ending on March 31, 2016 and March 31, 2017, wherein in each of the financial years, there was decline of approx. 50%. Though, in FY ending on March 31, 2017, the cash flow of ₹ 24,222 million has been observed from the proceeds from sale/ redemption of other Non-current Investments. This shows that IL&FS was facing issues in monetizing its assets in the group companies.

d. The Debt Equity ratio of the IL&FS on consolidated basis was in the higher range during financial years 2015-16 to 2017-18. During, financial year 2015-16 and 2016-17, the increase in Debt Equity ratio was gradual, but same has risen at alarming level during financial year 2017-18. This shows that IL&FS debt burden was quite high and there was visible mismatch between its debt and equity portfolio.

e. The short term borrowing of IL&FS on consolidated basis was rising sharply during FY ending on March 31, 2016 and March 31, 2017. During FY ending on March 31, 2016 it rises by approx. 37% and during FY ending on March 31, 2017 by 32%. This shows that IL&FS reliance on short term borrowings was increasing at a rapid level.

f. Other important factor is rise in 'Current Maturities of Long Term Debt' during FY 2016-17 and FY 2017-18 of the IL&FS on consolidated basis, wherein rise of 51% was observed in FY 2016-17 and 25% in FY 2017-18. If same is seen in tandem with rise in Short Term Borrowings for IL&FS on consolidated basis as well as standalone basis for FY 2015-16 and 2016-17, it can be said that, long term maturities of IL&FS were being funded by short term borrowings. This finding also gets support from the slow pace of monetization of assets of the IL&FS and its group companies.

57. In view of the above, I note that financial parameters of the IL&FS and its group companies especially, short term borrowings, debt equity ratio, current maturities of long term debt, operating profit, monetization of assets etc., were not as conducive or healthy as assumed by the Noticee in its rating report or rating rationale.

58. The extracts from rating reports of the Noticee clearly show that key updates considered for *credit rating* of NCDs of IL&FS were not healthy since 2016 and further deteriorated during quarter ending on December, 2017. More particularly, the rating report dated March 23, 2018 given by the Noticee shows that several financial parameters of the IL&FS such as increasing debt level, increase in gear ratio, increase exposure of debt in group companies, subdued profitability level and slow pace of asset monetization were degrading and aptly visible. These factors, in themselves, were enough to raise flag in December, 2017 only. The extract from the said rating report are shown in the following table:

Issue	Mar – 16	Mar – 17	Dec – 17	Comments of ICRA
High Debt Level	₹13,754 crore, Gearing ratio – 2.89	₹12,977 crore, Gearing ratio – 2.60	₹15,709 crore, Gearing ratio – 3.04	Increase in gearing in the current fiscal driven by loans and advances to group ventures. Debt expected to remain high with the repayment of loans extended to ITNL and SPVs.
Loans and Advances to Group	₹3,377 crore	₹3904 crore	₹5,518 crore	Increase exposure in loans and advances to group companies.
Profitability	RoA: 1.5% & RoE: 6.02%	RoA: 1.93% & RoE: 7.85%	RoA: 1.45% & RoE: 6.00%	Profitability continues to remain subdued. The improvement in FY 17

				was on account of tax reversal and was one time in nature.
Asset Monetization Plans	Slow Progress: Divested the trustee business of Vistra for a consideration paid over FY16 and FY17	Divested 49% stake in 5 projects aggregating to ₹1,000 cr. Sale of ISSL announced in Mar-17.	Limited Progress in current fiscal. Target of ₹2,219 cr through 7 deals in FY 18 of which 1 deal aggregating to ₹150 cr completed in H1.	Progress continues to remain slow with one transaction closed during the fiscal; regulatory approval awaited for ISSL divestment.

59. Certain other important extracts from other rating rationales as given below also suggest the above assessment:

i. IFIN's asset quality reported a marked deterioration in FY2014, precipitated by the general economic stress. While the asset quality remained stable in FY2015, there has been further deterioration in following years. The company's gross Net Performing Asset (NPA) to Rs. 527 crore as on March 31, 2018 (5.3% of gross advances) from Rs 291 crore as on March 31, 2017 (3.30% of gross advances) owing to certain large sized slippages. (July 30, 2018)

ii. IL&FS's investment portfolio remains relatively illiquid with large investments in group companies engaged in long-gestation and capital-intensive projects. The company has a demonstrated track record of liquidating its investments at frequent intervals, though the progress in recent years has been slow. Going forward, considering the high leverage levels; IL&FS' rating will remain sensitive to its ability to monetize its assets in a timely manner, achieve commensurate returns on investments while also preventing any breach in limits (as mandated by regulations) on leverage levels. (November 03, 2017)

iii. ICRA has noted that the support provided to group companies in the recent past has been higher than expected levels, however the management plan to moderate the same over the next few quarters partly mitigates the associated risks. (November 03, 2017)

iv. Ability to manage comfortable asset quality on its portfolio remains critical. (April 21, 2017)

v. With greater exposure to infrastructure segment in last few years, a relatively riskier segment, and the migration to a stricter non-performing assets (NPA) recognition norm, the asset quality of IFIN saw some deterioration. (April 21, 2017)

60. The Noticee has claimed that it has evaluated all aspects while rating NCDs of IL&FS i.e. financials, asset quality, liquidity, institutional parentage, past record etc. and on the basis of the same it has maintained the rating of IL&FS as 'stable' up to August 06, 2018. The Noticee has also contended that, the SCN has cherry picked statements from the said rationale but it does not rely on other aspects that were considered along with disclosure of the risks to the credit profile. In this regard, I note that, from the abovementioned table and extracts from credit rationales with respect to Issuer / its Group companies, analyzed by the Noticee, it has been observed that IL&FS financial parameters or credit profile was not as greener as shown by the Noticee. In every rating rationale (from 2017 – 2018), the Noticee has mentioned that IL&FS/ IFIN asset quality, ability to monetize its assets in a timely manner, maintaining leverage levels, high concentration in group companies, etc. will remain sensitive /critical elements while rating the NCDs of ILFS's. There was considerable delay in monetization of assets by IL&FS as admitted by the Noticee in the rating rationales provided by it. Further, asset quality of group companies of IL&FS and expanded lending to its group companies by IL&FS has always remained a concerned area for the Noticee, while rating the securities of IL&FS and its group companies. I find that though the Noticee has shown its concern regarding aforementioned deteriorating financial factors on continuous basis in its rating rationales, it had not acted upon the same diligently while rating the NCDs of IL&FS. I, therefore, find that the Noticee has failed to exercise its duty to the investors at large and failed to intervene in the matter on time by downgrading the ratings of NCDs of IL&FS despite having knowledge of the deteriorating financials of the issuer.

61. The Noticee has claimed that while '*rating*' the issuer and its group companies, it placed reliance on centralized treasury operations managed by IL&FS, the brand-value and respect commanded by IL&FS and particularly its reputation in the execution of large-scale infrastructural projects; well-established banking relationships; governance framework; past performance and track record; and the standing of the statutory auditors. However, from the financial parameters mentioned above, lack of desired due diligence on the part of the Noticee is clearly visible.

62. I also note that RBI, in its letter dated November 22, 2018 to SEBI observed that the Noticee failed in analyzing the information received/ obtained by it, from the perspective of repayment capability, concentration risk, etc. RBI, in its letter dated November 22, 2018, *inter alia* stated that "*The CRAs had derived comfort from the institutional parentage of IFIN. An independent assessment of IFIN by the CRAs as a standalone entity with specific focus on the effectiveness of the prevailing governance systems and executive capability is not evidenced from the clarifications furnished… IFIN derived financial flexibility and resource raising ability solely by virtue of IL&FS parentage".* The said observations of RBI show that the Noticee has failed in implying independent professional assessment while '*rating*' the NCDs of IL&FS and placed undue weightage on institutional parentage. The approach of laxity and complacency of the Noticee has further been

highlighted by RBI in its letter dated November 22, 2018 to SEBI, wherein *inter alia* it had mentioned as follows:

"…..*The CRAs derived comfort from the liquidity profile of IFIN for positions as on March 31, 2017 and March 31, 2018 which generally reflected positive cumulative mismatches across time buckets for the short and medium term time horizons except for a cumulative mismatch of* Rs. *482 crores in the 1-2 months bucket as on March 31, 2018. In addition to this, unutilized working capital limits and undrawn bank lines aggregating to* Rs. *1151 crores and* Rs.*812 crores as on March 31, 2017 and March 31, 2018 respectively facilitated a better perception of the liquidity position of the entity amongst the CRAs. However, the expansion in exposure of IFIN to group entities during FY 2017-18 (by 33.14%) through transitory loans extended in order to accommodate the delay in disbursements from banks/ FIs were not examined by the CRAs from the perspective of repayment capability……*

…..The rating reliance was more on the commitments provided by the management on gradual reduction of such group exposures through monetizing and refinancing of these project debts at the underlying SPVs as well as the access to the shares treasury infrastructure of IL&FS by IFIN which failed to materialize beneficially…..

….. Further, relying on the reasons stated by IFIN for delay as technical in nature, no downgrade was initially effected by ICRA on the rating assigned to CPs. Subsequently, even though the same was recognized as a material event, the rating was not downgraded and continued to be A1+ as on September 3, 2018…..

…Most of the loans extended by IFIN were in respect of high ticket promoter funding and infrastructure loans with long gestation periods. Although the top 15 individual borrowers constituted around 30% of the total credit exposure of IFIN, the same was not examined by the CRAs from the perspective of concentration risk……"

63. The Noticee has claimed that report of RBI has not been provided to it during the instant proceeding. However, it may be noted that Enforcement Department of SEBI vide its e-mail dated August 09, 2019, forwarded the said letter of RBI along with the observations to the Noticee. The aforesaid observations of RBI being the regulators for other financial instruments such CP of IL&FS rated by the Noticee corroborate the charge as found in this case.

64. Further, the Noticee's argument that Auditor had not raised any concerns or red flag regarding the financial parameters of IL&FS and its group companies and therefore, it cannot be questioned on basis of financial parameters is out of context. I note that, a '*credit rating agency*' responsibility is to evaluate the credit profile of the issuer whose instruments it is '*rating'* and for assessing credit profile, it must exercise due diligence as expected from it and consider all the financial parameters independently and apply independent professional judgment in assessing the '*true'*, '*accurate'*, '*fair'* and '*appropriate'* credit rating as required under the CRA Regulations. I, therefore agree with observations of examination by SEBI that the Noticee, being a responsible *credit rating agency* registered with SEBI, should have anticipated the mounting credit risks, the stressed balance sheet position of IL&FS and placed the ratings accordingly to alert the market in advance regarding the deteriorating financial profile of the issuer.

65. In this case, the Noticee has placed its reliance on the judgment of Hon'ble SAT in the matter of *Brickwork Rating India Limited Vs SEBI in appeal No. 439 of 2018, para 6-9*. In this regard I note that, said judgment of Hon'ble SAT is case specific. It is noted that the said judgment has come to be passed in different set of facts and circumstances than present one. In *Brickwork Rating* case, in the facts and circumstance of that case as brought out in para 7 and 9 of the order dated June 03, 2019, it was found that the '*credit rating agency'* in that case exercised *due diligence*. The differentiating factors were that the company in question was continuously in dialogue with the investors of NCDs for reschedulement and same was considered. The facts and circumstances of the instant case are entirely different than those of *Brickwork Rating* case. I further note that in para 8 of the order dated June 03, 2019 the Hon'ble SAT has applied Regulation 24(7) in different context than that of the present one. Hon'ble SAT has not held the interpretation that in all circumstances the regulation should be applied as sought to be contended by the Noticee. In fact, Hon'ble SAT has very clearly held that provisions of Regulation 24(7) *"indicates that CRA is required to exercise due diligence in order to ensure that rating given is fair and appropriate".* The aforesaid findings in this order also find support from this interpretation.

66. In view of the aforesaid findings, the failure on the part of the Noticee is apparently vivid and obvious in this case. I, therefore, find that the Noticee, while assigning its credit rating to the NCD of IL&FS, failed to exercise proper skill, care and due diligence while discharging its responsibilities as a *credit rating agency* and violated the provisions of Regulation 24(7) and Clauses 4 and 8 of Code of Conduct of the CRAs read with Regulation 13 of CRA Regulations and is liable for penalty under Section 15HB of the SEBI Act.

67. For the purpose of adjudication of quantum of penalty it is relevant to mention that under section 15I of the SEBI Act imposition of penalty is linked to the subjective satisfaction of the Adjudicating Officer. The words in the section that "*he may impose such penalty*" are of considerable significance, especially in view of the guidelines provided by the legislature in section 15J. The factors stipulated in Section 15J of the SEBI Act, which reads as follows:-

15J - Factors to be taken into account by the adjudicating officer

While adjudging quantum of penalty under section 15-I, the adjudicating officer shall have due regard to the following factors, namely:-

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

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

(c) the repetitive nature of the default.

Explanation-

For the removal of doubts, it is clarified that the power of an adjudicating officer to adjudge the quantum of penalty under sections 15A to 15E,clauses (b) and (c) of section 15F, 15G, 15H and 15HA shall be and shall always be deemed to have been exercised under the provisions of this section.

68. Having regard to the factors listed in section 15J and the guidelines issued by Hon'ble Supreme Court of India in *SEBI Vs Bhavesh Pabari Civil Appeal No(S).11311 of 2013* vide judgement dated February 28, 2019, it is noted that from the material available on record, any quantifiable gain or unfair advantage accrued to the Noticees or the extent of loss suffered by the investors as a result of the default in this case cannot be computed. It is also a settled position that the factors under Section 15J are not exhaustive but are inclusive. It is also important to mention that IL&FS is a systematically important Non Deposit Accepting Core Investment Company. It is in the business of raising and holding public funds. The exposure of IL&FS, at the relevant times, was critical to the financial stability as its share in total exposure of banks to NBFC sector was fairly high. There was substantial public interest involved in the affairs of the IL&FS considering its importance for financial stability. Though there is no allegation of any mala *fide* on the part of the Noticee, the failure by the Noticee is blameworthy and serious considering the degree of responsibility bestowed upon it by the statute. Further, in the peculiar facts and circumstances of this case the default has occurred due to lethargic indifference and needless procrastination and laxity of the Noticee. Considerable reliance of investors and regulators on opinion of *credit rating agencies* as hallmark of creditworthiness of issuer and the rated instruments clearly outweighs any kind of lack of due diligence by the credit rating agencies. The law does not permit any allowance to be made for such lethargic indifference and needless procrastination as found in this case. The brazen failure as found in this case, had clearly defeated the purposes of the Regulations i.e. investor protection and orderly development of the securities markets. Considering the role and responsibility of the Noticee in these regards and important obligations cast upon it under the CRA Regulations, in my view, the default is grave and the gravity of this matter cannot be ignored. Therefore, no lenient view should be taken in this matter and the case deserves imposition of monetary penalty proportionate to the default as found in this case.

69. Considering all the facts and circumstances of the case and exercising the powers conferred upon me under section 15I of the SEBI Act read with rule 5 of the Adjudication Rules, I hereby impose a penalty of ₹25,00,000/- (Rupees Twenty-Five Lakh only) on the Noticee *viz.* ICRA Limited under section 15HB of SEBI Act. In my view, the said penalty is commensurate with the violation committed by the Noticee in this case.

70. The Noticee shall remit / pay the said total amount of penalty within 45 days of receipt of this order by way online payment on SEBI website at following tabs on SEBI website www.sebi.gov.in –

ENFORCEMENT -> Orders ->Orders of AO -> Pay Online or by way of using the web link https://siportal.sebi.gov.in/intermediary/AOPaymentGateway.html.In case you face any difficulties in payment of penalties, you may contact the support atportalhelp@sebi.gov.in .

71. The said confirmation of e-payment made in the format as given in table below should be sent to "*The Division Chief, EFD-DRA-II, Securities and Exchange Board of India, SEBI Bhavan, Plot no. C- 4 A, "G" Block, Bandra Kurla Complex, Bandra (E), Mumbai - 400 051*" and also to e-mail id:- tad@sebi.gov.in

1	Case Name	
2	Name of the 'Payer/Noticee'	
3	Date of Payment	
4	Amount Paid	
5	Transaction No.	
6	Bank Details in which payment is made	
7	Payment is made for(like penalties/disgorgement / recovery/ settlement amount and legal charges along with order details)	

72. In the event of failure to pay the said amount of penalty within 45 days of the receipt of this Order, recovery proceedings may be initiated under section 28A of the SEBI Act, 1992 for realization of the said amount of penalty along with interest thereon, inter alia, by attachment and sale of movable and immovable properties.

73. In terms of Rule 6 of the Adjudication Rules, copies of this order are sent to the Noticee and also to SEBI.

Date: December 26, 2019 **Santosh Shukla**

Place: Mumbai **Adjudicating Officer**