

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

IN COMPLIANCE WITH THE ORDERS DATED JULY 1, 2009 AND NOVEMBER 19, 2010 OF THE HON'BLE SECURITIES APPELLATE TRIBUNAL MADE IN APPEAL NO. 96 OF 2008 [HB STOCKHOLDINGS LIMITED VS. SECURITIES AND EXCHANGE BOARD OF INDIA AND OTHERS]

1. This Order is being issued in compliance with the Orders dated July 1, 2009 and November 19, 2010 passed by the Hon'ble Securities Appellate Tribunal (hereinafter referred to as the Hon'ble SAT) in Appeal No. 96 of 2008 [HB Stockholdings Limited vs. Securities and Exchange Board of India, DCM Shriram Industries Limited (hereinafter referred to as the company) and others]. The Hon'ble SAT, vide Order dated July 1, 2009, while disposing of the appeal, had observed as below:

“During the course of the arguments, it was put to Shri Shiraz Rustomjee learned counsel for respondent no. 1 whether the respondent Board would like to consider the memorandum of appeal and the response filed thereto by the respondents before this Tribunal as their respective representations and pass a reasoned order. This suggestion was made keeping in view the fact that the impugned communication does not contain reasons. The learned counsel for the respondent Board has sought instructions and states that, in the peculiar facts and circumstances of the present case, the respondent Board is agreed to consider the memorandum of appeal and the response of the respondents as their respective representations and pass a reasoned order. He has further clarified that in order to put an end to the issue, the Board shall not afford personal hearing to any of the parties. We are in agreement with the learned counsel for the respondent Board in this regard. However, the respondent Board shall be free to seek any further clarification, if it deems necessary, from any of the parties. It goes

without saying that none of the parties before us in this appeal shall be entitled to file any further representation before the respondent Board.....” .

2. Thereafter, while disposing of a miscellaneous application filed by HB Stockholdings Limited (hereinafter referred to as the complainant) in the aforesaid appeal, the Hon'ble SAT, vide Order dated November 19, 2010, directed SEBI to comply with its Order dated July 1, 2009 on or before March 31, 2011. The aforesaid appeal (which was disposed of by the Order dated July 1, 2009) was filed by the complainant challenging two letters of the Securities and Exchange Board of India (hereinafter referred to as SEBI) dated June 20, 2008 which were sent to the complainant and its counsel. The complainant had made certain complaints to SEBI against the company, its promoters and the promoter group in respect of allotment of warrants by the company to certain entities, who, according to the complainant were the promoters/promoter group of the company or persons acting in concert with them, and the subsequent allotment of shares to them against the share warrants so issued to them. After examining the complaints, SEBI, had, vide letters dated June 20, 2008, informed the complainant and its counsel that the complaints had been examined and that no violations of the provisions of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (hereinafter referred to as the Takeover Regulations) or the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as the SEBI Act) by the company had been noticed. The complainant was also informed that violation of Section 173 of the Companies Act, 1956 as alleged by it, had been referred to the Ministry of Corporate Affairs. The said letters were challenged by the complainant before the Hon'ble SAT, for the following relief:

- (a) “Pass an order setting aside the Orders dated 20.06.2008 passed by SEBI with respect to the complaints of the Appellant;*
- (b) Pass an order directing the Respondent No.1 (SEBI) & Respondent No.3 (BSE) to investigate and pass appropriate orders against the Respondent*

No.2, its Promoters, Directors, promoter group entities and persons acting in concert, for the violations committed by them detailed in this Appeal, including but not limited to cancelling the issue of 7,00,000 preferential warrants on 30.11.2007 and the underlying 21,00,000 shares carrying distinctive numbers 15298438 to 17398437, and pending the investigation and for a period of four weeks thereafter freeze the voting rights and listing permission on the shares allotted;

(c)

(d) ”

3. I have perused the memorandum of appeal filed by the complainant and other material on record. In the appeal memorandum, the complainant has stated that it is the largest shareholder of the company in the category ‘public shareholders’ with the shareholding of 24.08% and 27.38% (as on July 7, 2008) of the ‘expanded issued and paid up capital’ and ‘unexpanded issued and paid up capital’ of the company, respectively. The complainant states that the company is a public company, listed on the Bombay Stock Exchange Limited (hereinafter referred to as BSE) with an authorized share capital of ₹65,00,00,000/- (Rupees sixty five crores only) divided into 6,50,00,000 (Six crore fifty lakh shares) equity shares of ₹10/- each. The issued, subscribed and paid up share capital of the company as on September 30, 2007 ₹15,29,84,370/- divided into 1,52,98,437 equity shares of ₹10/- each. As per the appeal memorandum, the capital as on the date of filing the appeal was ₹17,39,84,370/- divided into 1,73,98,437 equity shares of ₹10/- each. The complainant further stated that the company was engaged in the business of manufacturing sugar and is also engaged in manufacture and production of alcohol, chemicals and rayon. It was also stated that on October 16, 2007, the board of directors of the company had passed a resolution for issue of 7,00,000 warrants (each warrant carrying a right to apply for 3 underlying equity shares of ₹10/- each) as proposed. The warrants were to be allotted on a preferential basis to six entities, namely, Divine Investments Private Limited, Gentech Chemicals Private Limited, Super Wares Private Limited, Quick Lithographers Private Limited, Versa Trading Limited and Shri

Tilak Dhar (Karta of Lala Bansi Dhar & Sons-HUF), forming part of the promoters/promoter group/persons acting in concert (PAC) and that the resolution approving the issue of warrants was to be adopted through postal ballot.

4. The complainant had stated that the reason for the proposed preferential issue as contained in the Explanatory Statement to the Notice dated October 18, 2007 was to augment the long term working capital of the company and contends that the same could not be the real intent behind the said issue, as the company had availed loans to the tune of ₹87.572 crores during April 2007-April 2008. According to it, the company has not deliberately opted for a rights issue which allows the participation of all shareholders and instead opted for the preferential issue to the promoters and the promoter group. The complainant also stated that on November 3, 2007, 7,00,000 warrants (each carrying three underlying equity shares) were issued and allotted by the company to the aforesaid six entities. Pursuant to the same, the underlying shares were allotted in the following manner:

- i. 7,00,000 shares on December 18, 2007;
- ii. 4,55,000 equity shares on March 29, 2008 and
- iii. 9,45,000 shares on April 1, 2008.

The complainant has contended that the company was in the process of issuing and allotting 7,00,000 warrants and 21,00,000 shares underlying the said warrants, and that the acquiring entities of the promoter group along with the directors and promoters of the company have violated the provisions of the Takeover Regulations, the Securities and Exchange Board of India (Disclosure and Investor Protection) Guidelines, 2000 (hereinafter referred to as the DIP Guidelines), the Securities Contracts (Regulation) Act, 1956 (hereinafter referred to as SCRA), the Securities and Exchange Board of India (Prohibition of

Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 (hereinafter referred to as the PFUTP Regulations) and the Companies Act, 1956.

5. In terms of the Order dated July 1, 2009, the memorandum of appeal filed by the complainant before the Hon'ble SAT and the responses of the respondents therein, have to be considered by SEBI for passing a reasoned order. This Order, shall therefore dispose of the issues raised by the complainant in its memorandum of appeal, in compliance with the above mentioned Orders of the Hon'ble SAT. SEBI was also granted liberty to seek any further clarifications, if it deems necessary, from any of the parties concerned.

6. Pursuant to the Order of the Hon'ble SAT dated July 1, 2009, SEBI had ordered an investigation in the matter. As permitted by the Hon'ble SAT, information on paragraph-wise comments along with supporting documents were sought from the company with regard to the averments/submissions made by the complainant in its appeal memorandum. The complainant was also advised to furnish documents/evidence (other than what was already furnished by it along with the appeal memorandum) in support of its averments/allegations made in Para IV of its appeal memorandum titled '*Violation of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003*'. While the company replied and made its submissions, the complainant informed that it had no further documents to submit. I have perused the allegations in the appeal memorandum, the responses received from the company and other entities, the findings of the aforesaid investigation and other material available on record. According to the complainant in its memorandum of appeal, the following were the violations alleged to have been committed by the company, its directors, promoters and promoter group companies:

- i. Violation of Regulation 11(1) of the Takeover Regulations;
- ii. Violation of Regulation 23(1) of the Takeover Regulations;
- iii. Violation of the DIP Guidelines;
- iv. Violation of the Listing Agreement with the BSE and the provisions of SCRA;
and
- v. Violation of the PFUTP Regulations

The findings/observations on each of the allegations are given in the succeeding paragraphs.

A. VIOLATION OF THE PFUTP REGULATIONS:

7. The complainant has alleged that the company, its promoters and directors, along with other group companies, Versa Trading Limited and DCM Hyundai Limited had “executed *a fraud*” on the public shareholders of the company by issuing preferential warrants and the underlying shares. It stated that a grand design to unlawfully raise the promoter holding in the company at a deflated price by way of issuance of warrants was made. The company had denied the said charge and stated that the allotment of warrants and equity shares on preferential basis were made in full and formal compliance with all applicable laws. The complainant had, in its memorandum of appeal, stated that upto September 2002, Versa Trading Limited was admittedly a wholly owned subsidiary of the company and remained so as on date (the date of the appeal memorandum). It was also stated that during September 2002, the company had offloaded 50.02% of the shareholding in Versa Trading Limited for a pittance of 10 paise per share as against its acquisition price of ₹10/- per share to three entities, namely, AKS International, RPG Securities and Indus Netlink and that the said entities did not show their investment in Versa Trading Limited and therefore appeared to be benami holders. The company, had in its response to SEBI, submitted that Versa Trading Limited ceased to be its subsidiary in September 2002. It further submitted that the sale price for the equity shares of

Versa Trading Limited was reflective of its value at that time. It also stated that the complainant's grievance in connection with the preferential allotment had no relevance with the allegation that the shares of Versa Trading Limited were sold for a pittance. It further contended that there was no basis to allege that the transferees were "*benami holders*". The company also submitted that the copies of the Annual Reports of those entities sourced from the website of the Ministry of Corporate Affairs (MCA) provided the details of investments made by the companies (AKS International, RPG Securities and Indus Netlink) in Versa Trading Limited. It was further informed that in the Annual Report of RPG Securities, the investment in shares was classified under "Stock-in-Trade" and not "investment" and that the same could be the reason why the Report did not specify the 'company wise list' of investments and reiterated that it (the company) did not have any connection with any of the said three entities. In this regard, I note that in the appeal memorandum, it has been stated by the complainant in paragraph IV(i) that Versa Trading Limited, earlier known as DCM Shriram Leasing and Finance Limited, is a wholly owned subsidiary and remains so even as on date. However, in the subsequent paragraphs, the complainant has stated that the company offloaded 50.02% of its shareholding in the said entity in 2002 and balance of 49.98% was also sold during 2007-08. Therefore, both these averments clearly contradict each other. As stated earlier, when the company offloaded 50.02% stake in Versa Trading Limited, the said entity ceased to be a wholly owned subsidiary of the company in 2002. Further, the complainant has alleged that 50.02% shares of Versa Trading Limited were sold for a pittance of 10 paise per share. In this regard, it is noted that the company has furnished a copy of resolution no. 2(ii) passed by the Committee (in its meeting held on September 21, 2007) constituted by its Board for reviewing/approving disposal of unproductive assets wherein it was informed by Mr. Tilak Dhar, the chairman of the company, that the Committee in its meeting held on September 25, 2002 had approved divestment of 22.51 lakh equity

shares of DCM Shriram Leasing and Finance Limited (Versa Trading Limited) for a total consideration of ₹2.25 lacs shares @ ₹0.10 per share and that the book value of the equity shares of Versa Trading Limited was ₹(-)10 per share. Further, the board in its meeting held on January 23, 2007 had taken note of the intention of the company to exit from Versa Trading Limited fully. It is also noted that, as per the resolution, the company had also received a proposal from DCM Hyundai Limited to acquire the remaining 22,49,017 shares @ ₹ 0.10 per share which was the same rate at which the earlier lot was disposed off. Therefore, having regard to the aforesaid facts, and in the absence of any material to support the allegations of fraud, it would not be possible to arrive at any adverse inference on the conduct of the company in off-loading the shares of Versa Trading Limited. Further, as regards the charge that the purchasers of shares were “*benamis*”, it is noted from the annual reports (furnished by the company) of those companies that their purchases of shares of Versa Trading Limited are reflected therein. The investment of the said three entities has been reflected in their annual statement and not held secret. In view of the above, and in the absence of other material to support the said allegations, it cannot be held that the said entities are benami holders of the company.

8. The complainant has also alleged (in paragraph IV(iii) at page 34 of the appeal memorandum) that the sale price of the balance 49.98% held by the company in Versa Trading Limited, claimed to have been sold in 2007-2008, was not mentioned. The complainant had also stated that it was strange on the part of the company to sell its shareholding in Versa Trading Limited when it knew that about ₹18 crores would be raised by Versa Trading Limited for investment into the company itself. The company in its response has stated that the allegation that Versa Trading Limited would raise ₹18 crores for investment into the company as a grand design hatched in 2002 in order to make a subscription in 2007, was ‘far fetched’ and ‘fanciful’. It has not been brought out

by the complainant as to how the funds raised in the year 2002 would be utilised for an investment in 2007. It appears that this allegation is far fetched. Further, it is noted that the company had sold the remaining 22,49,017 shares (constituting 49.98%) @ ₹0.10 per share to DCM Hyundai Limited. As such sale/purchases and the timing thereof, are part of appropriate business decision making in a company and also in the absence of any other evidence to support any fraud or unfair act, it would not be possible to infer any malafide.

9. The complainant in paragraph IV(iv) at page 34 of the appeal memorandum, has averred that the company claimed that, out of the debt, a sum of ₹7 crores was converted into redeemable non-cumulative preference shares and that no date for conversion is given in this regard. It was alleged by the complainant that the said claim is a sham which was evident from the fact that the director's report dated July 30, 2007 of the company and that of Versa Trading Limited did not reflect any increase in authorized capital of Versa Trading Limited nor the issuance of any preference shares in lieu of the debt to the company. In reply to the said charge, the company has submitted as follows:

“The conversion of debt of Rs.7 Crores into Preference shares was effected on 30.07.2007. In a nutshell, the sequence of events is as follows:

- (a) VTL (a wholly owned subsidiary of DSIL at that time) as a result of losses suffered, defaulted in repayment of public deposits and in debt servicing towards banks from which it had borrowed loans for its business. The Hon'ble Company Law Board (“CLB”) by an Order dated 18.2.1999 approved a Scheme for repayment of deposits u/s 45 Q (2) of the RBI Act. As per the said Order, any shortfall in meeting the deposit liability of Rs.8.16 Crores was to be borne by its holding company i.e. DSIL.*
- (b) In order to meet the payment obligations on the deposits as arising out of such Order, DSIL provided advances on various dates from 1998-1999 to 2004-2005 totaling to Rs. 5.31 Crores to VTL in compliance with CLB Order. The dues towards depositors as per the CLB Order were fully discharged and an Affidavit to the effect was filed with CLB on 09.08.2004.*

- (c) Apart from the above, during the said period, amounts due from DSIL as a guarantor for the borrowings of VTL to Oriental Bank of Commerce (Rs. 122.40 Lakhs), State Bank of Indore (Rs. 105 Lakhs) and State bank of India (Rs. 95.34 Lakhs) aggregating to Rs. 322.74 Lakhs were also paid by DSIL, being the holding company of VTL.*
- (d) The total exposure of DSIL on account of VTL namely towards repayment of deposits and discharge of bank guarantees was Rs.7.8 Crores as on 2005-2006. Such amount therefore represented the debt due and payable by VTL to DSIL as on 31.3.2005.*
- (e) Because of the continued slump in the leasing business the Board of Directors of DSIL decided to exit from the leasing business and divested its control over VTL in Sept 2002 by selling 50.02% equity shares to three entities at a token consideration of Rs. 0.10 per equity share.*
- (f) Thereafter the balance 49.98% equity shareholding held by DSIL in VTL was divested by DSIL in favour of DCM Hyundai Limited. With effect from 12.10.2007, DSIL ceased to be a shareholder in VTL.*
- (g) With effect from 30.7.2007, substantial part of the debt due to DSIL from VTL was converted into preference shares and the balance amount of Rs.80 lacs was repaid. The Board of Directors of DSIL felt that such a conversion of debt on a non cumulative basis or a preference share capital, redeemable in ten years was a prudent decision for DSIL.”*

I have perused the said submissions. It is noted that the company, during the investigation, had furnished a copy of an Order dated February 18, 1999 of the Hon'ble Company Law Board (CLB) approving a scheme of repayment. From a perusal of the same, it is noted that the holding company of Versa Trading Limited i.e. the company would make good the shortfall of funds for making repayments as per the scheme. Therefore, according to the company, it, as the holding company was bound by the order of CLB to make payments to Versa Trading Limited for meeting its obligations. Accordingly, the company had made payments as a guarantor of fund since 1998-99 aggregating to ₹853.87 lakhs. As informed by the company, the conversion took place on July 30, 2007. As regards the complainant's allegation of "sham" and the non-reporting of the same in the director's report dated July 30, 2007, it is seen that the conversion of

debt into preference shares was done on July 30, 2007 i.e. during the year 2007-08 and the same has been reflected in the annual accounts of the company for the year 2007-2008. Since, the reporting cannot precede the investment; no adverse inference could be drawn. As regards, the non-reflection of increase in the authorised capital of Versa Trading Limited, it is noted that the said entity is an unlisted company and hence for the said lapse, if any, it is not under the regulatory purview of SEBI.

10. Further, the complainant in paragraph IV(v) at page 34 of the appeal memorandum, has alleged that in the Annual Return (dated August 30, 2007) of Versa Trading Limited filed with the Registrar of Companies, does not reflect the increase in the share capital or the issuance of preference shares to the company. The complainant has also provided the shareholding pattern according to the said annual return and the same is reproduced below:

No.	Entity	Number of shares	Percentage
1.	DCM Shriram Industries Limited	22,49,011	49.98
2.	S. G. Nair	1	-
3.	Ravi Bahadur	1	-
4.	B. P. Khandelwal	1	-
5.	N. K. Jain	1	-
6.	Raj Kurnar	1	-
7.	K. K. Srivastava	1	-
8.	AKS International Ltd	7,50,000	16.67
9.	RPG Securities & Financial Services Limited	7,50,000	16.67
10.	Indus Netlink Limited	7,51,000	16.67
Total		45,00,017	100

According to the complainant, all the six individuals shown as shareholders in the table above are employees, either of the company or of its wholly owned subsidiary, Daurala Foods and Beverages Limited. The complainant has stated that the remaining three entities, namely AKS International Limited, RPG Securities and Financial Services Limited and Indus Netlink Limited, together

hold 50.02% of the shareholding of Versa Trading Limited and alleged that from the Annual Returns and Auditor's Report of these three companies for the years ending March 31, 2006 and 2007, it was seen that none of the entities mentioned their investment in Versa Trading Limited and therefore appear to be benami holders. I find that the said allegation of the entities being benamis has already been dealt above and as brought out above no inference could be drawn to establish such allegation. The complainant has also alleged that as per the Auditor's Report for the year ending March 31, 2007, the accumulated losses of the company have exceeded the company's share capital and reserves by ₹6.53 crores, which is more than fifty per cent of its net worth and these factors raised "*substantial doubt that the company will be able to continue as a going concern*". In response to the same, the company had stated that the auditor's observation about having a doubt as to whether the company can be a going concern had no bearing on the allegations made by the complainant in the proceedings. I have considered the allegation and the submissions made by the company. As I find that the said allegation bears little relevance to the issue of warrants itself, I do not wish to dwell any further on the said issue.

11. As regards paragraph IV(vii) at page 36 of the appeal memorandum, it has been stated that on September 25, 2007, resolutions were passed at the annual general meeting of the company for creating security for loans of ₹36 crores availed of during 2007. The company has submitted that the same has no relevance to the matter. Resolution for creating security for loans availed is a business decision of the company and in the absence of any other material to establish malafide in that regard, I find that the same cannot lead to any adverse inference.

12. The complainant has also alleged (in paragraph IV(viii) at page 36 of the appeal memorandum) that, on October 16, 2007, the board of the company passed a resolution to issue 7 lakh warrants to the Promoters/Promoter Group

companies including Versa Trading Limited and that eventually Versa Trading Limited was allotted 6.9 lakh warrants for ₹18.63 crores. According to the complainant, the same was done despite the fact that Versa Trading Limited had a negative net worth; was prohibited by Reserve Bank of India (RBI), vide order dated November 24, 2001 directing it not to transact the business of a non-banking financial institution; and was not authorized by its Memorandum of Association (MoA) and Articles of Association (AoA) to make such investments. The complainant also stated that the minutes of the meeting further indicated that rights issue was never discussed, and that the Letters of Intent had been received by the proposed allottees including Versa Trading Limited. With respect to the said averments, the company submitted the following:

“The information sought in relation to para IV (viii) of the Appeal are all contained in the Explanatory Statement to the Resolution under Section 81 (IA) of the Companies Act, 1956 passed by the shareholders of DSIL approving the Preferential Issue of capital. The said notice spells out all the terms of the Issue.

Specifically it may be noted that the pricing, as approved by the shareholders of DSIL under Section 81(IA) of the Companies Act, was to be decided by the Board of DSIL or the Sub-committee of the Board as per the resolution subject to the applicable provisions contained in the SEBI (Disclosure and Investment Protection) Guidelines, 2000 (“DIP Guidelines”)

We may mention that the Sub-committee constituted by the Board vide its resolution dated 16.10.2007 had resolved the price at Rs.57 per equity shares of Rs.10 each, which was 10% higher than the price arrived at as per the formula provided in the DIP Guidelines in its meeting held on 08.11.2007. Meanwhile, the market price of shares of DSIL increased and the Sub-committee of the Board on 21.11.2007 taking into account various circumstances revised the price upward to Rs.90 per share, which was 70 % higher than the price as per the said Guidelines. Such upward revision reflected intermittent increase in the market price and was in the interest of DSIL.”

I have considered the aforesaid submissions. From the reply, it is noted that the company had preferred the preferential allotment route to raise finance. As long as the statutory requirements are complied with by a listed company for raising

funds by whatever mode legally available to it, the company cannot be faulted for choosing a particular mode. It is in the wisdom of the company and its shareholders/board to adopt an appropriate mode for raising capital for the company. It is noted that the Board of Directors of the company in their meeting held on October 16, 2007, approved the proposal to issue upto 7 lakh warrants on preferential basis to the promoters/promoter group/persons acting in concert with them conferring a right to apply and subscribe upto 21 lakh equity shares of ₹10 each for cash. A notice under Sections 81(1A) and 192A(2) of the Companies Act, 1956 was issued by the company and a special resolution dated November 26, 2007 was also passed through postal ballot under Section 192A of the Companies Act, 1956. The shareholders of the company had consented to the said issue as more than 82% shareholders' votes were in favour of the said issue. The investigation had found that only after the same, were the allotments made. Further, pursuant to the receipt of the entire amount due on the warrants upfront, the warrants were converted into equity shares and issued to the allottees in three tranches. As regards the other allegations against Versa Trading Limited, it is reiterated that the said entity is an unlisted company and as such, I would not be able to go into the veracity of these.

13. In paragraph IV(ix) at page number 36 of the appeal memorandum, the complainant has also stated that on October 18, 2007, a notice was sent to the shareholders stating that the purpose of the issue was to raise working capital and for supplementing bank finance and that there was no mention of payment of cane arrears. Further, according to the complainant, the said notice does not state the number of warrants to be allotted to each of the six proposed entities. It was stated that the amount proposed to be raised was approximately ₹12 crores. The complainant has further, in paragraph IV(xviii) at page 40 of the appeal memorandum, stated that the company has time and again changed the stated purpose (as reproduced below) for which the warrants were issued:

	Reasons for the issuance of warrants as stated in the Notice dated 18.10.2007	Reasons for the issuance of warrants as stated in the Letter dated 06.11.2007 to the Petitioner	Reasons for the issuance of warrants as stated in the Reply to the Petition in CLB
1.	Augment the long term working capital of the Company	Requirement of funds to service the restructured and other long term debt	Urgent need of funds for the payment cane price arrears of almost 12,000 cane growers amounting to ₹12 crores
2.	Supplement the Bank finances	For meeting normal capital expenditure	Service the restructured and other long term debt
3.		For modernization/ expansion of projects in hand	For meeting normal capital expenditure
4.			For modernisation / expansion of projects in hand

The company had stated, in response, that there was no deviation of any nature from the purpose for which the issue was made. It further stated that the purpose for issuance of warrants was set out in the Notice (to the shareholders) dated October 18, 2007 and the Explanatory Statement thereto issued to the shareholders and none of the clarificatory or elaborative reason set out in the letter to the complainant or in the reply filed in the CLB proceedings, were inconsistent with the contents of the purpose set out in the Explanatory Statement for shareholder approval under Section 81(1A) of the Companies Act, 1956. According to the company, the payment for cane arrears is also a working capital liability and as such was not required and mentioned specifically in the notice. It further stated that the object of the Issue as set out in the Explanatory Statement clearly stated that the Issue was warranted because of the crisis situation faced by the sugar industry especially in Uttar Pradesh due to the mismatch in the cane price and the selling price of sugar prevalent at that time. It also informed that the names of the entities of the promoter group to whom the warrants were proposed to be issued and the total number of warrants to be issued were clearly stated in the Postal Ballot Notice and that the right of the proposed allottees to the warrants was therefore joint and several. Therefore, according to the company, there was no requirement of giving the number of warrants to be subscribed by individual entities at that stage. The said allegation made by the complainant and the submissions made by the company are noted.

I note that the investigation in the matter has observed that the company is a diversified company with operations *inter alia* in sugar and that since cane being a raw material in the production process, any expenditure incurred in the procurement of the same would constitute part of the working capital needs of the company. Further, though the payment for cane arrears was not specifically mentioned in the notice, the explanatory statement to the notice had mentioned that the mismatch in cane price and the selling price had led to crisis situation and *“In order to augment long term working capital of the company in the present situation and to supplement bank finances, it is proposed to issue on preferential basis.....”*. The end use of the funds to be raised was disclosed to the shareholders who had voted in majority in the postal ballot in favour of the proposal to raise finance by way of preferential allotment to the promoter group of the company. As regards the number of warrants to be issued to each of the six entities, it is observed from the notice that the shareholding patterns of the company before and after allotment of the shares were given detailing the names of the entities and the aggregate allotment to be made to the proposed allottees. Since the entities have been classified as belonging to the promoter group, not mentioning of the number of warrants to be allotted separately to each of them, cannot alone be a sole basis for finding the company culpable.

14. In paragraph IV(x) at page number 37 of the appeal memorandum, the complainant has stated that it had on October 25, 2007, wrote a letter to the company seeking an explanation for the preferential issue proposed by the Company and the rationale for not considering a rights issue and that the company had replied vide its letter dated November 6, 2007 stating *“It has to be borne in mind that a rights issue not only involves avoidable costs but in the present sugar scenario is not a good proposition.”* Apart from problem due to over production, high cane price and low sugar price, the Govt. had started issuing Recovery certificates for non-payment of cane price arrears. The High Court which was seized of

the matter also ordered issue of RCs to the Sugar Mills. The relief expected from the State and Central Govt. were not forthcoming.” It is the grievance of the complainant that the letter was at variance with the terms of the notice dated October 18, 2007 given to the shareholders. The company stated that there is no inconsistency in the letter from the company to the complainant and the Notice to the shareholders under section 81(1A) of the Companies Act, 1956 seeking approval for the Preferential Issue of capital. According to the company, its reply to the complainant dealt with the contents of the complainant’s letter to the Company and that the notice to the shareholders dealt with all the requirements of disclosures to be made under Section 173 of the Companies Act, 1956 and the DIP Guidelines. As regards the complainant seeking the rationale from the company for not considering a rights issue, it is already observed above that the company on approval by its shareholders could decide on the legally available mode to raise capital. The company had replied to the complainant that a rights issue involved a certain financial burden and informed it of the recovery certificates being issued towards the cane arrears. Further, the shareholders have voted in favour of the preferential allotment to warrants which were subsequently converted into equity. Therefore, in view of the aforesaid reasons and circumstances, I am of the opinion that the company, in the facts and circumstances, cannot be faulted for adopting the preferential allotment route for raising capital and proceeding with the same after due approval by its shareholders.

15. In paragraph IV(xi) at page number 37 of the appeal memorandum, the complainant has further alleged that on October 31, 2007, November 2, 2007 and November 6, 2007, it had requested for an opportunity to inspect the Register of Members and a copy thereof but received only a copy after the filing of a company petition on November 21, 2007 before the Hon’ble CLB. In respect of this averment, I note that the investigation had found from the records that the

complainant had initially sought inspection of the said register on October 31, 2007 and was advised by the company on November 1, 2007 that the same could be inspected by an authorized person at the office of its registrar, Karvy Computershare Private Limited, New Delhi. It is noted that the complainant had visited the said office. But as it was satisfied with the records that were shown and subsequently, on November 6, 2007 the complainant sought a list of beneficiary holders of the company in the depository system *inter alia* containing the addresses of the shareholders and appears to have paid the cost as indicated by the company. Thereafter, the complainant has admitted of having received a copy of the Register of Members. Though, the company could have shared a copy of the register of members as soon as it received a request in that regard from the complainant, I observe that it did so eventually.

16. The complainant has also stated in paragraph IV(xii and xiii) at page numbers 37 and 38 of the appeal memorandum, that on November 15, 2007, Versa Trading Limited had passed three resolutions at an extra-ordinary general meeting (EGM) to (a) increase its authorized capital to ₹32 crores, (b) issue and allot 2 crore equity shares of ₹10/- each to DCM Hyundai Ltd., which is referred to as its holding company, and (c) obtain approval of shareholders under S. 372A(1) for the purpose of making an investment of ₹18.63 crores for subscribing to “6.9 lakh warrant at ₹90/- per share” issued by the company. It is the case of the complainant that as on October 16, 2007, the Letter of Intent given by Versa Trading Limited to the company to subscribe to the proposed issue of warrants was without authority and hence void. The complainant has further alleged that as per the company, the price of the warrants was revised only on November 21, 2007 to ₹90/- per share from ₹57/- previously fixed on November 8, 2007. Therefore, according to the complainant, it was strange that Versa Trading Limited would have offered to subscribe to warrants at ₹90/- per share on November 15, 2007 when the company’s board meeting determined

this price only on November 21, 2007. According to the complainant, the previous price fixed by the board of the company was ₹57/- per share vide resolution dated November 8, 2007 and that it was a case where documents were being created to justify the allotment of warrants. The complainant has further averred that on November 21, 2007, the board of directors passed a resolution fixing the price of each underlying share at ₹90/- per share, which was an increase from ₹57/- per share fixed earlier in the meeting held on November 8, 2007. It is the submission of the complainant that this factum would not, in the normal course, have been known to Versa Trading Limited on November 15, 2007, when it passed a resolution to acquire the warrants at ₹90/- per underlying share. With respect to the aforesaid, the company had submitted that it was the allottees who had accepted the company's proposal to increase the price which had resulted in the board committee approving the revision in price from ₹57/- to ₹90/- per share on November 21, 2007. It was also stated that the company and the proposed allottees were engaged with each other on the pricing of the preferential capital in the light of the increase in the market price. According to the company, the proposed allottee was perfectly right in passing an enabling Resolution stating there the price at which the shares are to be subscribed and that there was no inconsistency in the board of the company deciding the price on November 21, 2007 and in Versa Trading Limited passing an enabling resolution on November 15, 2007 stating the price. As the company had informed that it engaged itself with the proposed allottees (including Versa Trading Limited) on the pricing of the instruments to be allotted on preferential basis in the light of the increase in the market value, I am unable to arrive at any adverse finding on the same. With respect to the charge that the letter of intent of Versa Trading Limited given on October 16, 2007 was void as the enabling resolution was passed only on November 15, 2007, I find that as the said entity is unlisted, SEBI does not have any regulatory authority on such companies on

such issues unless the same has any bearing on the securities market. This is not so in the present case.

17. The complainant has also stated (in paragraph IV(xiv) at page 38 of the appeal memorandum) that on November 29, 2007, it again wrote to the company urging it to go for a rights issue and even offered to have the same underwritten. The complainant further stated that it made an offer to subscribe to the warrants proposed to be issued at a price of ₹120/- per share as against the price of ₹90/- that had been proposed. It is the grievance of the complainant that its letter was ignored completely and the warrants were allotted to the promoters. In reply, the company has stated that the complainant had pursued the remedy provided under Sections 397/398 of the Companies Act, 1956, alleging oppression and mismanagement by opting for Preferential Issue and not Rights Issue and the matter was pending before the Hon'ble CLB. The company has also informed that the complainant had also filed a Civil Suit before the Hon'ble Delhi High Court for the same allegations, which was dismissed with costs by an Order dated August 25, 2009. The Hon'ble High Court while dismissing had observed *"Here the Plaintiff first approached the CLB and failed to obtain any interim relief. It cannot be permitted to approach the civil court seeking the same relief as that would encourage forum shopping and constitute an abuse of the process of law.....Having carefully, examined the plaint as well as the averments made in the petition before the CLB, as further sought to be amended by the subsequent application, it appears to this Court that the grounds on which the relief is being sought for are more or less similar to what has been sought in the CLB....."* It was also informed that the petition filed by HB before the CLB is pending. On appeal, the Division Bench of the Delhi High Court had declined to interfere in the matter. As it has been informed that the matter is pending before the Hon'ble CLB, the issue is *sub-judice*. SEBI would as a regulator, intervene only when the interests of the shareholders are in any manner adversely affected

because of the acts of the company. As in the present matter, the shareholders have voted in majority for the allotment of warrants to the promoter group on preferential basis, SEBI would have no adverse remarks on the mode adopted by the company for mobilising capital for its working needs. As regards the offer of the complainant to subscribe to the warrants at a price of ₹120/- per share as against the price of ₹90/-, I would refrain from recording my observations here, as according to the company, the same is pending adjudication by the Hon'ble CLB.

18. The complainant has also stated in paragraph IV (xv) at page 39 of the appeal memorandum that on November 30, 2007, 7 lakh warrants (including 6.9 lakh warrants allotted to Versa Trading Limited) were allotted by the company completely ignoring the complainant's letter dated November 29, 2007 and even when the matter was to be heard by the Hon'ble High Court on the same day. The complainant further alleged that ₹18.9 crores was raised despite the fact that as per the Notice dated October 18, 2007, the company required only ₹12 crores and that the company ought to have reduced the number of warrants issued. It was also averred that no evidence of actual receipt of money to the tune of ₹18.90 crores was shown except for an auditor's certificate and there was no information as to the utilization of the money allegedly raised for payment of cane arrears. According to the complainant, the same was obviously false as loans were raised from the Sugar Development Fund and Banks for that specific purpose. As regards the said allegations, the company had submitted that nowhere in the notice it was mentioned that the Preferential Issue was to raise ₹12 crores only and that the same appeared to be an assumption of the complainant. The company further submitted that a statutory duty was cast on the auditors to verify and report on the utilization of capital raised and the same was done in the 'CARO Report' annexed to the Auditors Report for the year 2007-08. The company had stated that the proceeds were credited to the

company's current account maintained with Axis Bank Limited and the proceeds were used for working capital requirements including payment of cane arrears. According to the company, as part of prudent fund management, the funds were kept in liquid temporary investment in mutual fund units which were withdrawn from time to time. I have examined the said submissions. The investigation had observed that the notice to the shareholders did not state that the company required ₹12 crores. As regards the allotment of 7 lakh warrants (including 6.9 lakh warrants allotted to Versa Trading Limited) by the company, I note that the same has been challenged by the complainant before the Hon'ble CLB and therefore the same is sub-judice. The company has furnished copy of its bank statement during the investigation evidencing the receipt of ₹18.90 crore and also a certification from the bank to this effect, in addition to the auditor's certificate. Therefore, it may not be correct to state that the company was not in receipt of the issue proceeds. As regards the utilization of the money, the company has furnished tabulated details pertaining to the utilization of funds by it *inter alia* for the purpose of cane payments substantiated with relevant bank statements. In view of the same, I am unable to arrive at any adverse finding against the company on this.

19. The next averment by the complainant in paragraph IV (xvi) at page 39 of the appeal memorandum was that the warrants were to be converted into equity shares in three tranches and that as per the notice dated October 18, 2007 for postal ballot, the second tranche of equity shares would be issued between April 1, 2008 and March 31, 2009 and the third and final tranche after April 1, 2009. It is the allegation of the complainant that the company went ahead and issued the entire number of underlying equity shares by April 1, 2008. In reply to the said charge, the company submitted that the original proposal required the subscribers to pay only 10% of the offer price initially and the remaining 90% within 18 months as permitted under the DIP Guidelines. It

submitted that the said condition was provided in terms of 'Issue in compliance with the DIP Guidelines', though the intention was to collect the subscription early according to the fund requirements. According to the company, as the Hon'ble CLB had put a condition that the entire consideration should be paid in advance at the time of subscription to the warrants, the allottees paid full consideration for the equity shares in advance. It is the submission of the company that as full consideration was paid in advance as per the Order of the Hon'ble CLB, at the request of the subscribers to the warrants, the Board/Committee of Directors in exercise of the powers delegated by the Special Resolution of the shareholders dated November 26, 2007, allotted first tranche of 7 lakh equity shares on December 18, 2007; the second tranche of 4.55 lakh equity shares on March 29, 2008; and remaining 9.45 lakh equity shares on April 1, 2008. I have taken note of the said submissions. The investigation has observed on a perusal of the notice for the postal ballot, that the resolution contained a provision authorizing the Board to *inter alia "take all actions and to do all such acts, deeds, matters and things as it may, in its absolute discretion, deem necessary..... to settle all questions, difficulties or doubts that may arise while implementing the proposal i.e. the proposed issue, offer and allotment of the Warrants and Equity shares arising therefrom, including change in the period for exercise of option subject to relevant guidelines....."* Further, the conversion of warrants was authorised by the shareholders and also since the entire subscription was received in advance in compliance with the Order of the Hon'ble CLB, I am unable to find any lapse or irregularity in the allotment of shares before the scheduled period. Therefore, no adverse inference can be drawn in this regard.

20. The complainant has also alleged in paragraph IV (xvii) at page 39 of the appeal memorandum that on March 26, 2008, a resolution was passed by the Board of Directors of Versa Trading Limited stating that it is now a wholly owned subsidiary of DCM Hyundai Limited. It was further stated therein that DCM

Hyundai Limited has proposed to extend its financial year by 6 months, and Versa Trading Limited resolved to extend its own financial year by 6 months as well. According to the complainant, this was an obvious attempt by the respondents (said companies) to try to hide and/or delay the auditor's report of the companies as far as possible given the current litigation. In this regard, I note that the said averments relate to Versa Trading Limited and DCM Hyundai Limited, where both are unlisted companies. Since the said companies do not come under the regulatory purview of SEBI, in respect of such activities, no observations are made. The complainant has further stated (in paragraph IV (xix) at page 40 of the appeal memorandum) that during August 2007 to April 2008, the company had availed of ₹87.752 crores from Sugar Development Fund and a consortium of Banks, of which ₹45.752 crores was raised specifically for the purpose of payment of sugarcane arrears. As regards the said averment, the company has stated that a company was free to pursue and raise resources from various sources to meet ongoing working capital expenses. It further submitted that availing of one source does not preclude raising funds from another source. I have noted the submissions. As I find that the said decision is a business decision of a company for raising funds, I shall not deal with the same any further.

21. The complainant, in its appeal memorandum (in paragraph IV (xx and xxi) at page 40 and 41), has also stated that the company held 49.28% shareholding in DCM Hyundai Limited along with 100% of optionally convertible preference shares amounting to ₹12.85 crores and that the Articles of Association of DCM Hyundai Limited gives substantial control to the company over the management and composition of the board of directors. Further, the Chairman and Managing Director of DCM Hyundai Limited, one Alok Shriram, is the Deputy Managing Director and Promoter of the company. According to the complainant, the said facts indicate that DCM Hyundai Limited is a subsidiary of the company. The

complainant has further stated that DCM Hyundai Limited has pledged all its movable and immovable properties to the company, which has undertaken to repay all its loans to banks and financial institutions. It is also stated that DCM Hyundai Limited has been a loss making company since 1995, and was declared "Sick" by the Board for Industrial and Financial Reconstruction (BIFR) on July 28, 1998, and is currently under a scheme of rehabilitation sanctioned by the BIFR in 2007. Further, according to the Director's Report of DCM Hyundai Limited, the company has written off loans of over ₹75 crores in the company. In this regard, the company has denied that DCM Hyundai Limited was its subsidiary. I find that in the absence of any material, no inference to the contrary can be drawn. Further, as observed above, DCM Hyundai Limited, being an unlisted company, SEBI's regulatory jurisdiction does not extend to such entities, in respect of the alleged acts.

22. The complainant further alleged in paragraph IV (xxii) at page 41 of the appeal memorandum that the company first finances Versa Trading Limited and DCM Hyundai Limited and then subsequently writes off crores of dues from both the companies, thereby depleting shareholder value. According to the complainant, inspite of such writing off, the said companies still owe crores of outstanding dues to the company. The complainant has also alleged that instead of these dues, DCM Hyundai Limited purportedly bought 49.98% shareholding of the company in Versa Trading Limited and 50.02% shareholding from three benami entities. The complainant further stated that DCM Hyundai Limited has extended ₹20 crores to Versa Trading Limited to subscribe to warrants issued by the company all the while being under a scheme of rehabilitation sanctioned by the BIFR. In the case of Versa Trading Limited, the complainant has stated that the said entity while still owing money to the company has subscribed to 6.9 lakh warrants allotted by the company. In response to these allegations, the company has submitted that the allegation that the management is depleting its share

value, is baseless. According to the company the said allegation was raised by the complainant in various fora and so the called “grand scheme and design” is a figment of imagination of the complainant. As already stated above in this Order, in terms of a CLB Order, the company had to make good the shortfall of funds to enable Versa Trading Limited for making repayments. Therefore, accordingly, the company has made payments as guarantor, since 1998-99 aggregating ₹853.87 lakhs. Therefore, no adverse inference can be drawn about the financial assistance provided to Versa Trading Limited. Further, Versa Trading Limited and DCM Hyundai Limited are unlisted companies and do not fall under the regulatory purview of SEBI, in the context of the allegations stated above.

23. In conclusion, the complainant has alleged that the sham transactions described in its appeal memorandum (as also dealt with in this Order) amounted to a fraud played by the company, its directors and promoters, on the public shareholders including the complainant in relation to the securities issued by the company to its promoters group entities, the alleged money received, and the purpose and utilization of the proceeds. The company has denied the said allegations. As observed above, on the basis of the documents and the evidence furnished by the parties, and also those on record, the allegations of the complainant are not substantiated. Therefore, no violations of the provisions of the PFUTP Regulations, lie against the company.

B. ALLEGED VIOLATION OF REGULATION 11(1) OF THE TAKEOVER REGULATIONS:

24. The complainant has alleged that the allotment of 7,00,000 warrants by the company on November 30, 2007 as well as the allotment of 21,00,000 shares underlying such warrants (in three tranches, i.e., 7,00,000 equity shares on December 20, 2007, 4,55,000 equity shares on March 29, 2008 and 9,45,000 equity shares on April 1, 2008) to its promoters/promoters’ group/PAC has been

done in gross violation of Regulation 11(1) of the Takeover Regulations. The complainant had stated, in its memorandum of appeal that SEBI and BSE was intimated of the allotment to the promoter group despite the pendency of the legal proceedings initiated by it before the CLB. The complainant has stated that, even as per the company in its notice dated October 18, 2007, the said allotment would result in an increase of 8.14% in the voting rights of the entire promoters/promoter group/PAC from 32.54% to 40.68% of the equity capital of the company. It was also stated that the promoters/promoter group/PAC had exercised their option to convert the warrants to equity shares by paying the consideration on November 30, 2007. The complainant has alleged that 'the allotment of warrants on November 30, 2007 was in violation of the provisions of Regulation 11(1) of the Takeover Regulations', as it resulted in an increase in the 'shares' held by Promoters/promoter Group/PAC, which would entitle them to exercise more than 5% of the voting rights in the company, as the said acquisition causing such increase was made in the same financial year. The complainant has averred that since the promoters/promoter group/PACs already held 32.54% voting rights in the company and since the same was done by warrants, the allotment of warrants was also bad in law. The complainant has also stated that the company has not deliberately opted for rights issue so as to allow participation of all shareholders and instead opted for a preferential issue.

25. In this regard, the following questions arise for my consideration.

- a. Whether the allotment of 21,00,000 shares (underlying 7,00,000 warrants) was in violation of Regulation 11(1) of the Takeover Regulations?
- b. Whether the company can be faulted for taking the 'warrants' route instead of a rights issue for raising capital for the company?

26. I note from the notice dated October 18, 2007 issued by the company to its shareholders to pass a resolution to offer and issue not exceeding 7,00,000

warrants, on preferential basis, entitling the warrant holder(s) to apply for three equity shares per warrant (in the following time frame- one share on or before March 31, 2008, one share between April 1, 2008 and March 31, 2009 and one share on or after April 1, 2009 but before 18 months from the date of allotment of the warrants, to the promoter/promoter group/persons acting in concert with them, whether or not they are members of the company). The explanatory statement dated October 18, 2007 has mentioned *“In order to augment the long term working capital of the Company in the present situation and to supplement Bank finances it is proposed to issue on Preferential basis to the Promoters/Promoter group/Persons Acting in Concert with them, in accordance with the Guidelines for Preferential Issues contained in Chapter XIII of the Securities and Exchange Board of India (Disclosure and Investor Protection) Guidelines, 2000 (“the Guidelines”) as amended by Circular dated January 25, 2005 and April 30, 2007, upto 7 lac Warrants, entitling the warrant holders to apply for three Equity Shares per Warrant.....”*. It was also mentioned that an amount equivalent to not less than 10% of the price fixed for the equity shares has to be paid along with the application for allotment of warrants and allotment of warrants shall be made within fifteen days of passing of the resolution and that the said amount would be adjusted against the issue price of the respective equity shares when allotted. I note that the allottees to whom warrants were allotted, had exercised their option to apply for equity shares and that 21,00,000 equity shares against those warrants had been allotted to them on various dates during the financial years 2007-2008 and 2008-2009.

27. The allotment of warrants does not in any way entitle the allottees to exercise voting rights in the company. Warrants do not themselves carry any voting right in the company. Voting rights/shareholding would accrue only on the conversion of such warrants into equity shares. Thus, the allottees would be entitled to exercise voting rights only upon conversion of the warrants into equity

shares. Also, the explanatory statement dated October 18, 2007 issued to the shareholders had mentioned in clear terms that *“The Warrants shall have no voting or dividend rights attached to them”*. Therefore, mere issue of warrants on preferential basis to the promoters/promoter group and the persons acting with them, by the company cannot violate Regulation 11(1) of the Takeover Regulations. An acquisition would become bad under Regulation 11(1) of the Takeover Regulations only when the acquirer fails to make the public announcement as mandated thereof, when he acquires such percentage of shares or voting rights as mentioned therein. The complainant has alleged that the allotment of 21,00,000 shares of the company to the allottees was in contravention of Regulation 11(1) of the Takeover Regulations, as the allottees/acquirers and the promoter group as a whole, did not make the mandatory public announcement. Therefore, it needs to be examined whether the acquisition of 21,00,000 equity shares by the allottees (forming part of the promoter group) required them to make a public announcement. Since, the issue pertains to the applicability of Regulation 11(1) of the Takeover Regulations; the same is reproduced hereinbelow for reference.

“Consolidation of holding

11 (1) *No acquirer who, together with persons acting in concert with him, has acquired, in accordance with the provisions of law, ¹[15 per cent or more but less than ²[fifty five per cent (55%)]] of the shares or voting rights in a company, shall acquire, either by himself or through or with persons acting in concert with him, additional shares or voting rights entitling him to exercise more than ³[5% of the voting rights],¹[with post*

¹ Substituted for "not less than 10% but not more than 51%" by the SEBI (Substantial Acquisition of Shares and Takeovers) (Amendment) Regulations, 1998, w.e.f. 28-10-98.

² Substituted for "75%" by the SEBI (Substantial Acquisition of Shares and Takeovers) (Amendment) Regulations, 2005, w.e.f. 3-1-2005

³ Substituted for "10% of the voting rights" by the SEBI (Substantial Acquisition of Shares and Takeovers) (Second Amendment) Regulations, 2002, w.e.f. 1-10-2002. Earlier it was substituted for "5% of the voting rights" by the SEBI (Substantial Acquisition of Shares and Takeovers) (Third Amendment) Regulations, 2001, w.e.f. 24-10-2001.

acquisition shareholding or voting rights not exceeding fifty five per cent.,] ²*[in any financial year ending on 31st March] unless such acquirer makes a public announcement to acquire shares in accordance with the regulations.*

(2).....
.....”

28. There is no dispute regarding the fact that the promoter group of the company was holding 32.54% of the total equity capital of the company as on September 30, 2007 i.e prior to the allotment of shares underlying 7,00,000 warrants allotted on November 30, 2007. The allottees as mentioned above in this Order, form part of the promoter group. The information on the ‘shareholding pattern’ of the company for the quarter ending December 2009, as available in the website of BSE also supports the fact that the allottees are shareholders belonging to the “Promoter and Promoter Group”. As the allottees had exercised their option on the warrants and have been allotted shares underlying such warrants, it needs to be first seen whether the acquisition by the allottees (forming part of the promoter group) have entitled the promoter group to exercise 5% of the voting rights in any financial year ending and if yes, then to find whether a public announcement as required under the said regulation had been made or not. Even according to the company (in its explanatory statement dated October 18, 2007), pursuant to the full allotment of equity shares, the promoters holding would increase from 32.54% to 40.68%, an increase by 8.14%. The company had issued 7,00,000 warrants to its promoter group entities on November 30, 2007 and that the 21,00,000 equity shares underlying such warrants were allotted on various dates during 2007-2008 and 2008-2009, as given below:

¹ Inserted by the SEBI (Substantial Acquisition of Shares and Takeovers) (Third Amendment) Regulations, 2009, w.e.f. 6-11-2009.

² Substituted for the words “in any period of 12 months” by the SEBI (Substantial Acquisition of Shares and Takeovers) (Second Amendment) Regulations, 2002, w.e.f. 9-9-2002.

DATE OF ALLOTMENT	FINANCIAL YEAR	NO. OF SHARES ALLOTTED (UNDERLYING THE WARRANTS)
December 18, 2007	2007-2008	7,00,000
March 29, 2008	2007-2008	4,55,000
April 1, 2008	2008-2009	9,45,000

29. With this increase in the shareholding of the promoter group, pursuant to the allotment of shares, the next step would be to ascertain whether the said increase had entitled them to enjoy more than 5% voting rights in the company in the end of the financial year. The first tranche of allotment of 7,00,000 shares was done on December 18, 2007 during the financial year 2007- 2008. Again, during the same financial year (on March 29, 2008) 4,55,000 shares were allotted to the entities forming part of the promoter group. Thus, the total number of shares allotted to the promoter group entities was 11,55,000 shares during 2007-08. In view of the said allotment, the total issued capital of the company, in terms of number of shares had increased from 1,52,98,437 shares to 1,64,53,437 (1,52,98,437+11,55,000=1,64,53,437). The number of shares held by the promoter group before the allotment was 49,81,992 shares (constituting 32.75%), which includes certain market purchase. On account of the allotment of 11,55,000 shares during the year 2007- 2008, the holding of the promoter group had increased to 61,36,992. The shareholding/voting rights of the promoter group pursuant to the said acquisition was 37.30% $(61,36,992 \times 100 / 1,64,53,437)$ i.e. an increase of around 4.84%, which was below the 5% level (for the financial year 2007-2008), as stipulated under Regulation 11(1) of the Takeover Regulations.

30. The third tranche of 9,45,000 equity shares were allotted to the promoter group on April 1, 2008, during the financial year 2008-2009. On account of the said issue of shares, the total capital of the company rose from 1,64,53,437 shares to 1,73,98,437 shares. The said allotment had increased the

shareholding of the promoter group entities to 70,81,992 shares. Pursuant to the said acquisition, the shareholding/voting rights of the promoter group entities had increased to 40.70% $[70,81,992 \times 100 / 1,73,98,437]$. i.e an increase of 3.40% which was again within the specified limit of 5%. Therefore, from the given facts and the applicable provisions of law, it can be inferred that increase in the promoter group's shareholding was well with the threshold limits. Therefore, it can be held that the promoter group had not violated the provisions of Regulation 11(1) of the Takeover Regulations, while acquiring the shares of the company in the financial years 2007-2008 and 2008-2009. In view of the above, the said allegation would not sustain and is therefore rejected.

31. The complainant also stated that it had informed SEBI of the acquisition of 11,00,342 equity shares of the company by the promoters of the company through Pearey Lall & Sons Private Limited (6,83,794 shares) and M/s. A Cee Enterprises (4,16,548 shares). The complainant has alleged that both the said entities are persons acting in concert (PAC) with the promoters/promoter group of the company. According to the complainant, a director in Pearey Lall & Sons Private Limited was also a director in certain group companies and that the above mentioned acquisitions had increased the voting rights of the promoter/PAC even beyond 8.14% (pursuant to the allotment of shares underlying the warrants) as contended, once again without a public announcement in violation of Regulation 11(1) of the Takeover Regulations. While examining the said allegations, I note that Pearey Lall & Sons Private Limited has been mentioned as a shareholder of the company in the category *"Public and holding more than 1% of the total number of shares"*, in the 'shareholding pattern' of the company for the quarter ended December 2009, data as available in the website of BSE. I also note that, vide letter dated March 17, 2008, Pearey Lall & Sons Private Limited informed SEBI that it was just a shareholder of the company and there is no other relation or connection with it. The entity also

mentioned in the said letter that it has no relationship or connection with M/s A Cee Enterprises. The complainant has also alleged M/s. A Cee Enterprises to be a PAC of the promoter group. In this regard, M/s. A Cee Enterprises, vide its letter dated March 14, 2008 informed SEBI that it had purchased shares of the company during November 2007 from the market and that apart from being a shareholder of the company, it denied having any other relationship/connection either with the company/its promoters or with Pearey Lall & Sons (E.P.) Limited. In view of the above reasons and in the absence of adequate material from the complainant, it would be difficult to hold Pearey Lall & Sons Private Limited and M/s. A Cee Enterprises, to be PACs of the promoter group. Further, for the reasons stated above in this Order, the promoter group was not be liable to make a public announcement in respect of their acquisition of shares underlying the warrants.

32. As regards the second issue raised in paragraph 25 above – *whether the company/its promoters can be faulted for resorting to the 'warrants' issue instead of a rights issue*; I note that the allotment of warrants to the promoter group entities had been approved through a postal ballot. Further, the objective of the warrants issue was to augment long-term working capital of the company and to supplement bank finances. One observation is that the warrants have been converted into equity shares before the schedule for the conversion as mentioned in the notice to the shareholders. However, the same was provided for in the draft resolution that the Board was *inter alia* authorized to change the period for exercise of option subject to relevant Guidelines, etc. without being required to seek any further consent or approval of members. I note that the entire amount for the allotment of warrants was received upfront and subsequently the underlying shares on those warrants had been issued by the company to such allottees. As the shareholders have consented to this aforesaid manner of raising funds, SEBI would not be concerned as to the mode of raising

capital; the only requirement being that the same is done in accordance with law. The complainant seems to have been affected by the said issue of warrants and the allotment of equity shares underlying such warrants to the promoter group, seen in the background of its grievance of 'oppression and mismanagement' against the company and its complaints made to the CLB under Sections 397 & 398 of the Companies Act, 1956. As long as the method resorted to by a public listed company in raising capital is legally recognised and done in accordance with the applicable laws, SEBI would refrain from probing the method or manner adopted for raising capital.

C. VIOLATION OF REGULATION 23 OF THE TAKEOVER REGULATIONS:

33. The complainant has alleged that the allotment of 7,00,000 warrants by the company to its Promoters/Promoters Group/PAC on November 30, 2007, was in violation of the provisions of Regulation 23(1)(b) of the Takeover Regulations. The basis for the said allegation was that the allotment of warrants and the shares underlying such warrants were issued by the company during the offer period of the public announcement made by the complainant. The complainant has stated that Regulation 23(1) of the Takeover Regulations mandates that after a public announcement has been made, the directors of the company are prohibited, during the offer period, from

a) selling, transferring, encumbering or otherwise disposing off or entering into an agreement for sale, transfer, encumbrance or for disposal of assets otherwise, not being sale or disposal of assets in the ordinary course of business, of the company or its subsidiaries,

b) issuing or allotting any authorized but unissued securities carrying voting rights during the offer period, and

c) entering into any material contracts, unless approval of the general body of shareholders is obtained in this regard.

34. According to the complainant, the only issue/allotment permitted during the offer period was limited to issue of shares upon exercise of option against warrants (issued prior to the date of the public announcement), as per the pre-determined terms of conversion or exercise of option. It appears that the complainant had made a public announcement on November 19, 2007, and the date of closure was initially on January 24, 2008. As per the complainant, the allotment of warrants by the company to the promoter group entities was on November 30, 2007, which was subsequent to its public announcement and was therefore in violation of Regulation 23(1)(b) of the Takeover Regulations.

35. Here, the issue to be determined is whether the issue of warrants by the company was in violation of Regulation 23 of the Takeover Regulations. For ease of reference, Regulation 23 of the said regulations is reproduced herein below:

“General obligations of the board of directors of the target company

23. (1) *Unless the approval of the general body of shareholders is obtained after the date of the public announcement of offer, the board of directors of the target company shall not, during the offer period,—*

(a) sell, transfer, encumber or otherwise dispose of or enter into an agreement for sale, transfer, encumbrance or for disposal of assets otherwise, not being sale or disposal of assets in the ordinary course of business, of the company or its subsidiaries; or

(b) issue 1[or allot] any authorised but unissued securities carrying voting rights during the offer period; or

(c) enter into any material contracts.

2*[Explanation.—Restriction on issue of securities under clause (b) of subregulation*

(1) shall not affect -

(i) the right of the target company to issue or allot shares carrying voting rights upon conversion of debentures already issued or upon exercise of option against warrants, as per pre-determined terms of conversion or exercise of option;

(ii) issue or allotment of shares pursuant to public or rights issue in respect of which the offer document has already been filed with the Registrar of Companies or Stock Exchanges, as the case may be.] ”

1 Inserted by the SEBI (Substantial Acquisition of Shares and Takeovers) (Second Amendment) Regulations, 2002, w.e.f. 9-9-2002.

2 Substituted *ibid.* Prior to its substitution, Explanation read as under:

“*Explanation.*— Restriction on issue of securities under clause (b) of sub-regulation (1) shall not affect the right of the target company to issue and allot shares carrying voting rights upon conversion of debentures already issued or upon exercise of option against warrants, as per pre-determined terms of conversion/ exercise of option.”

36. Under the aforesaid Regulation, the issue or allotment of any authorized but unissued securities carrying voting rights during the offer period shall not be made, unless the approval of the general body of shareholders is obtained after the date of the public announcement of the offer. The restriction on issue of securities shall not affect, *inter alia*, the right of the company to issue or allot shares carrying voting rights upon conversion of debentures already issued or upon exercise of option against warrants, as per pre-determined terms of conversion or exercise of options. The complainant had averred that Regulation 23(1)(b) of the Takeover Regulation allows the issue of shares under warrants during the offer period only if such allotment is made as per the pre-determined terms of conversion. According to the complainant, the terms of conversion, in the instant case, were altered without obtaining a specific approval of the shareholders. In this regard, I note from the Notice that the resolution contained a provision authorizing the Board to *inter alia* “*take all actions and to do all such acts, deeds, matters and things as it may, in its absolute discretion, deem necessary..... to settle all questions, difficulties or doubts that may arise while implementing the proposal i.e. the proposed issue, offer and allotment of the Warrants and Equity shares arising therefrom, including change in the period for exercise of option subject to relevant guidelines...*”. I further note that the special resolution passed by the shareholders by postal ballot, had authorized the board *inter alia* to change the period for exercise of option subject to relevant Guidelines, etc. without being required to seek any further consent or approval of members. The allotment of

warrants on preferential basis and the change in the period of conversion of warrants was authorized by the shareholders. Therefore, in view of the Order of Hon'ble CLB placing a condition therein that the entire consideration should be paid in advance at the time of subscription to the warrants, no adverse inference can be drawn. The entire amount for the allotment of warrants was received upfront and there being no legal restraint on the allotment of warrants/shares; the subsequent issue of shares underlying such warrants cannot be faulted. Further, in terms of the Explanation to Regulation 23, the restriction on issue of securities under clause (b) of sub-regulation (1) [of Regulation 23] shall not affect the right of the target company to issue or allot shares carrying voting rights upon conversion of debentures already issued or upon exercise of option against warrants, as per pre-determined terms of conversion or exercise of option. In view of the said reasons, it would be difficult to hold otherwise.

37. I note that the complainant has also contended that the company had entered into material contracts and executed agreements encumbering its assets, which again was in contravention of Regulation 23(1)(a) & (c) of the Takeover Regulations. In this regard, the company, vide letter dated August 8, 2008 informed SEBI that it has not sold transferred, encumbered or entered into any agreement for sale/transfer/encumbrance or disposal of assets during the offer period. It was also stated therein that the company routinely borrows funds from banks and Sugar Development Fund etc. for meeting the operational requirements and for such routine borrowings, charges are created on current assets as per the terms of borrowings. According to the company, such mortgages are always created with the approval of the shareholders under Section 293(1)(a) of the Companies Act, 1956 and the said borrowings are within the limits approved by the shareholders under Section 293(1)(d) of the Companies Act, 1956 by resolution passed in a general meeting. In view of the above submissions of the company and in the absence of any other document

suggesting contravention, I am unable to hold that the company had violated Regulation 23(1)(a) of the Takeover Regulations. Further, in terms of Regulation 23(1)(c) of the Takeover Regulations, unless approval of the general body of shareholders is obtained after the date of the public announcement of offer, the board of directors of the target company shall not during the offer period, enter into any material contracts. The complainant while alleging that the company was creating/entering into material contractual obligations without seeking approval of its shareholders, has not cited any particular instance of this. The company, as stated earlier, has submitted that it had not entered into any agreement for sale/transfer/encumbrance or disposal of assets during the offer period. In view of the above submissions of the company and in the absence of any other supporting document from the complainant's side, it cannot be inferred that the company has contravened 23(1)(c) of the Takeover Regulations.

D. VIOLATION OF THE DIP GUIDELINES:

38. The complainant has alleged that the said allotment is against Clause 13.3.1 (f) of the Guidelines as according to the said provision, no listed company shall make preferential issue of equity shares/warrants/convertible instruments to any person unless the entire shareholding of such persons in the company, if any, is held by him in dematerialised form. It is the case of the complainant that several entities/persons in the promoter group/PACs are holding physical shares of the company. In terms of the notice issued under Section 81(1A) of the Companies Act, 1956, warrants were allotted to 6 entities, namely, Tilak Dhar (Karta–Lala Bansi Dhar & Sons – HUF), Divine Investments Private Limited, Gentech Chemical Private Limited, Super Wares Private Limited, Quick Lithographers Private Limited and Versa Trading Limited, on November 30, 2007. During the investigation, a list of physical and demat shares held by the Promoters/ Promoter Group of DCM as furnished by the complainant was perused. It was noticed from the said document that shareholding of all the

6 allottees were in demat form. In view of the same, the allegation stands unsubstantiated.

39. Further, the complainant has stated that, in the notice and explanatory statement dated October 18, 2007 issued by the company under Section 192A of the Companies Act, 1956, no price at which the underlying shares were to be allotted, was specified and that only the formula as given under the Guidelines was mentioned. It was also stated that the directors of the company had failed to intimate the shareholders, the price of ₹57/- per share that was fixed by them on November 8, 2007 and also the subsequent upward revision of the price to Rs.90/- per share on November 21, 2007 was not communicated to the shareholders. It further submitted that the real reason for the said allotment was to increase the shareholding of the promoters/promoter group/PACs. According to it, the proposal was made in the garb of augmenting long term capital when on the other hand; in a general meeting held on September 25, 2007, it was authorized to take a loan of about ₹15 crores for the working capital. It alleged that the fact of subsistence of the open offer made by the complainant was not communicated to the shareholders. The complainant further alleged that even after the allotment of warrants and the first tranche of the underlying shares, the exact number of warrants and shares allotted to each entity forming part of the promoter group, was not intimated to the shareholders. In this regard, I note that Clause 13.1.2.1(a) of the erstwhile Guidelines only provides that where warrants were issued on a preferential basis, the issuer company shall determine the price of the resultant shares in accordance with clause 13.1.1.1 of the Guidelines. Further, clause 13.1.2.2 of the Guidelines further states that the special resolution to be passed in terms of Section 81(1A) shall clearly specify the relevant date on the basis of which price of the resultant shares shall be calculated. I further note that, in case of preferential allotment, neither the Guidelines nor Section 173 of the Companies Act, provide for specifying the

price at which the underlying shares will be valued. Further, there are no legal requirements for intimating any change in the pricing thereafter, as the price is determined on the basis of a relevant date. I also note that clause 13.5.1A of the Guidelines, states that the issuer shall place a copy of the certificate of its statutory auditor before the general meeting of the shareholders certifying that the issue is being made in accordance with the requirements of these regulations. Further, as regards the allegation of “*concealment of the real reason for the issuance of warrants*” I note that Clause 13.1A of the DIP Guidelines provides that the explanatory statement to the notice for the General meeting shall contain the objects of the issue through preferential offer. The object/reason as stated in the notice/explanatory statement is that the funds are intended for augmenting long term working capital for the company. It appears that veracity of the reason disclosed by the issuer company is being questioned. As already held above, no fault may be attributable for choosing the mode of raising the capital, when the same is done after the approval of the shareholders and in accordance with law.

40. As regards the allegation that even after the allotment of warrants and the first tranche of the underlying shares, the exact number of warrants and shares allotted to each entity forming part of the promoter group, was not intimated to the shareholders, I note that Clause 13.1A of the Guidelines, provides that the explanatory statement to the notice for the General meeting shall *inter alia* contain the object of the issue through preferential offer; the identity of the proposed allottees and the percentage of the post preferential issue capital that may be held by them etc. The company had in the notice/explanatory statement pursuant to Section 192A (2) and Section 173(2) of the Companies Act, 1956, had made disclosures regarding the identity of the proposed allottees. It was also stated that they belong to the Promoter/Promoter Group/Persons Acting in Concert. It was further stated that in the event of warrants remaining

unsubscribed by the Promoter/Promoter Group/Persons Acting in Concert, the board of the company may allot it at its absolute discretion to any other entity owned and controlled by the Promoter Group. As regards the disclosure of post issue holding, the issuer company had disclosed the same.

E. VIOLATION OF THE LISTING AGREEMENT AND THE PROVISIONS OF SCRA:

41. It has also been *inter alia* alleged that the company had not complied with Clause 19 and 24 of the Listing Agreement and Section 21 of the SCRA. According to the complainant, the company had also violated Clause 13.1B of the Guidelines. The complainant has stated that the same was brought to the notice of BSE and SEBI. It had also alleged that by not permitting all shareholders to participate in the issue, the company had also violated clause 23 of the listing agreement. The complainant further stated that the company had not obtained the approval/permission of BSE before issuing\allotting warrants and the underlying shares to the promoter group. It also averred that only post-facto intimation was sent to BSE regarding the allotment of warrants on November 30, 2007, where the exact number of warrants allotted to each allottee was not disclosed. As regards the charge against the company having violated Clauses 19, 23 & 24 of the Listing Agreement and Section 21 of the SCRA, I find that a 'listing agreement' is entered into by an issuer company and a recognised stock exchange for the purposes of listing the company and for matters connected therewith. The compliance with the various requirements as envisaged under the listing agreement is supervised by the stock exchange (BSE in this case). Further, BSE is one of the respondents in the appeal filed by the complainant. In the present case, BSE had granted in-principle approval. Further, the company had obtained the shareholders approval in respect of the issuance of warrants to the promoter group. Therefore, in the absence of

anything to the contrary, it has to be inferred that there is no violation of clauses 19, 23 and 24 of the listing agreement and Section 21 of the SCRA.

42. The allegations made by the complainant in its memorandum of appeal have been examined in the light of replies/documents furnished by the parties, the findings of investigation and other material available on record, and findings/observations in respect of the same have been recorded in the earlier paragraphs. A summary of such findings/observations are given below:

- i. The allegation of the complainant that the company, its promoters and directors along with companies, Versa Trading Limited and DCM Hyundai Limited have executed a fraud on the shareholders of the company by way of issuing preferential warrants and underlying shares thereby contravening Regulation 3 of the PFUTP Regulations, has not been substantiated by the findings of the SEBI investigation and from the averments/documents of the complainants. Further, the business activities/decisions of unlisted entities like Versa Trading Limited and DCM Hyundai Limited would be outside the regulatory purview of SEBI unless the same becomes prejudicial to the interest of the investors and the securities market. However, the SEBI investigation and the documents furnished by the complainant could not substantiate that the acts of the said entities had affected the securities market in general and the shareholders of the company in particular.
- ii. The allegation of violation of Regulation 11(1) of the Takeover Regulations is not proved as the acquisition by the promoter group was well within the threshold limits under the said provision during the financial years – 2007-2008 and 2008-2009.
- iii. Pearey Lall & Sons Private Limited and M/s. A Cee Enterprises cannot be held to be the PACs of the promoter group for want of material in that regard and also since they have been classified as shareholders of the

company under the category “Public and holding more than 1% of the total number of shares”.

- iv. The company cannot be faulted for raising capital through preferential allotment of warrants overlooking a rights issue. The said mode was a decision of the company and the shareholders had voted in majority.
- v. The alleged violation of Regulation 23 of the Takeover Regulations is not found as the company has issued equity shares underlying the warrants which are in line with the terms of the explanation to the said provision. As regards the allegation that the company has entered into material contracts and encumbered its assets, the same is rejected on the basis of the submissions of the company, as mentioned above and also for want of material to support such a charge.
- vi. There is no contravention of clause 13.3.1(f) of the DIP Guidelines as the allottees of warrants were holding shares of the company in dematerialised form. Further, the violation of other provisions of the DIP Guidelines as alleged by the complainant is also not substantiated for the reasons stated in this Order.
- vii. BSE has granted in-principle approval for the issue of equity shares (underlying the impugned warrants). The shareholders of the company have approved the preferential allotment to six of the persons/entities of the promoter group. No violation of the provisions of the Listing Agreement as alleged in the appeal memorandum and also Section 21 of the SCRA could be inferred.

43. In view of the foregoing, I am of the considered view that the findings and observations made in this Order with respect to the allegations made by the complainant in its memorandum of appeal do not call for any regulatory intervention by the Securities and Exchange Board of India in the matter.

44. With the above observations, the representation made by the complainant, HB Stockholdings Limited in its memorandum of appeal (in Appeal No. 96 of 2008 – HB Stockholdings Limited vs. Securities and Exchange Board of India and others) is hereby disposed of in compliance with the Orders dated July 1, 2009 and November 19, 2010 passed by the Hon'ble Securities Appellate Tribunal.

DR. K. M. ABRAHAM
WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA

PLACE: MUMBAI
DATE: MARCH 31, 2011