

IN THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No.100 of 2007

Date of Decision: 18.10.2007

HFCL Infotel Ltd. **..... Appellant**

Versus

Securities and Exchange Board of India **.....Respondent**

Present : Shri Somashekar Sundaresan, Advocate alongwith Shri Vinay Chauhan, Advocate for the appellant

Shri J. J. Bhatt, Senior Advocate alongwith Ms. Daya Gupta, Advocate and Ms. Chloris John, Advocate for the respondent

CORAM

Justice N.K. Sodhi, Presiding Officer
Arun Bhargava, Member
Utpal Bhattacharya, Member

Per: Justice N.K. Sodhi, Presiding Officer (Oral)

Whether the draft offer document presented by the appellant to the Securities and Exchange Board of India (for short “the Board”) for its comments should be allowed to be withheld is the short question which arises for our consideration in this appeal filed under Section 15T of the Securities and Exchange Board of India Act, 1992 (for short “the Act”). The Board by its order dated 7.3.2007 has ordered the same to be withheld till proceedings against the appellant and Himachal Futuristic Communications Limited and others are concluded under Section 11B of the Act. Facts giving rise to this appeal may first be noticed.

2. HFCL Infotel Ltd. (transferor company) was an unlisted company incorporated under the provisions of the Companies Act, 1956. In March, 2003, it merged with Investment Trust of India Ltd. which is a listed company. It is common case of the parties that the merger has been approved by the High Court of Punjab and Haryana and also by the High Court at Chennai. The merged entity retained the name of the transferor company, that is, HFCL Infotel Ltd. (hereinafter referred to as "Infotel"). Himachal Futuristic Communications Ltd. (for short "Himachal") holds 61.98% of the shares of Infotel. Himachal is a public limited company in which about 98% shares are held by the general public. In pursuance to the aforesaid scheme of amalgamation, the transferee company (Investment Trust of India Ltd.) issued in March, 2003, 43,20,00,250 equity shares of Rs.10 each to the shareholders of the transferor company. These shares have not been listed since then. After the amalgamation, Infotel approached the Bombay Stock Exchange (for short "BSE") for listing the aforesaid shares allotted to the shareholders of the transferor company. The matter regarding the listing of the shares was placed before the listing committee of the BSE in its meeting held on July 29, 2003 and that committee noted that there were hardly any disclosures available for the investors which were otherwise required to be made by Infotel for listing under IPO guidelines. According to the committee, such disclosures were imperative especially when the unlisted company with a large capital was merging with a listed company with a relatively smaller capital. BSE decided that Infotel should undertake an offer for sale to raise the shareholding of non promoters to the minimum level required as per the Securities and Exchange Board of India (Disclosure and Investor Protection) Guidelines, 2000 (for short "the guidelines"). BSE communicated its decision as per letter dated

11.8.2003. It appears that further discussions/representations were made to the BSE for getting the aforesaid shares listed. BSE reiterated its earlier stand that Infotel should make an offer for sale and this is what it communicated to the appellant as per its letter dated November 11, 2004:

“2. In this connection, it has been observed that the present listed capital of the company is Rs.10.45 crores, whereas additional capital of Rs.432.00 crores are to be listed on amalgamation. Thus a large capital of unlisted company gets listed on the Exchange without any disclosures to the prospective investors.

3. The Exchange after considering the facts in the matter, decided that listing of additional 43,20,00,250 equity shares issued pursuant to the scheme of amalgamation would be listed only after company makes an Offer for Sale as intimated in the Exchange letter no. List/smg/km/2003 dated 11th August, 2003.”

It appears that BSE was insisting that the promoters of Infotel should sell 25% of their holdings in the market before the application for listing of the shares could be taken up. Feeling aggrieved by this action of BSE, Infotel filed Appeal no.7 of 2005 before this tribunal. During the pendency of the appeal, the issue was settled amicably between the parties and the appeal was not pressed. BSE then by its letter dated November 2, 2005 communicated to the appellant that its promoters should divest atleast 1.33% of the paid up share capital to the Indian public within six months by way of an “offer for sale” in the domestic market. The relevant part of this letter reads as under:

“Please refer to your application for listing of 43,20,00,250 equity shares issued pursuant to the scheme of amalgamation approved by the Hon’ble High Court of Punjab & Haryana and to the hearing held on September 27, 2005 before the Securities Appellate Tribunal (SAT) wherein SAT advised to place your matter before the Listing Committee for its consideration.

2. In this regard we refer to the appearance of Mr. Sanjeev Vashistha (General Manager and Company Secretary), Mr. Vikas Agarwal (Dy. General Manager, Corporate Finance) and Mr. Vinay Chauhan (Advocate) before the Listing Committee on October 6, 2005 wherein it was agreed that:

.4.

a) Promoters will divest atleast 1.33% of the paid up share capital to the Indian public within 6 months of the Listing Committee meeting i.e. on or before April 5, 2006 by way of Further Public Offer or an Offer for Sale in the domestic market. Any other way of dilution by way of GDRs/ADRs/FCCBs will not be considered as dilution for meeting the said requirement of non-promoter holding:

As per the requirements of BSE, the promoters of Infotel had to divest 1.33% of the paid up share capital to the Indian public within six months. In view of this condition, Infotel prepared a draft offer document and sent it to the Board for its comments as required by the guidelines. This application remained pending for quite some time and since an applicant is required to furnish the financial data for a period of six month immediately preceding the filing of the application, Infotel after regular intervals continued filing revised letters of offer updating its financial data. The application has been disposed of by the Board by its order dated March 7, 2007 with an observation that “the draft offer for sale document filed by HFCL Infotel Ltd be withheld till the proceedings under section 11B of the SEBI Act are disposed of”. It is against this order that the present appeal has been filed.

3. It is pertinent to mention here that the Board had ordered investigations into the buying, selling and dealing in the shares of Himachal for the period from October, 1999 to March 31, 2001. Investigations revealed that Himachal, its promoters and subsidiaries had provided funds and shares to one Ketan Parekh and entities connected with him and thereby aided and abetted them to manipulate the price of the scrip thereby violating the provisions of Regulation 4 of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995. It is not in dispute that in view of the findings of the investigations a show cause notice dated August 30, 2004 has been issued to

Himachal and its promoters and subsidiaries to show cause why suitable directions under Sections 11 and 11B be not issued restraining them from accessing the capital market. Investigations also revealed that Infotel – the appellant herein had given Rs.65 crores to Goldfish Computers, said to be a Ketan Parekh entity and the same was received back in August, 2000. The appellant has also been served with a show cause notice dated August 30, 2004 to show cause why appropriate directions be not issued to it under Section 11B restraining it from accessing the capital market. Ketan Parekh and some of the companies controlled by him have been found by the Board to be scamsters who rigged the securities market in a big way in the year 1999-2000 and by order dated 12.12.2003 they have been debarred from associating with the securities market for a period of 14 years. This order was affirmed by this Tribunal on 14.7.2006. On receipt of the show cause notice, Himachal has filed a writ petition in the High Court at Delhi challenging the jurisdiction of the Board to proceed against it which stands admitted and further proceedings before the Board have been stayed. Although there is no stay order against the appellant, the Board is not proceeding against it since Himachal and its subsidiary companies including the appellant are being dealt with together.

4. We have heard Shri Somashekar, Advocate on behalf of the appellant and Shri J.J. Bhatt, learned senior counsel on behalf of the Board. More than 43 crore shares were allotted by the transferee to the shareholders of the transferor company in pursuance to the scheme of amalgamation which stands approved by the respective High Courts. Even though the shares were allotted in March 2003 they have not been listed so far. It is for the listing of these shares that Infotel filed an application with the BSE and, as noticed earlier, the

condition imposed by the latter is that the promoters of Infotel should divest themselves of at least 1.33% of the paid up share capital in the domestic market in favour of the Indian public. Admittedly, Himachal holds about 62% of the shares in Infotel and it has agreed to divest 1.33% of the total paid up share capital by offering them to the public in the domestic market in terms of the conditions imposed by the BSE. A draft letter of offer is pending with the Board the consideration of which has been withheld pending enquiry pending against Himchal, the appellant and others under Section 11B of the Act. Is this action of the Board justified in the circumstances of the case is the question for our consideration. In the normal circumstances we would not have interfered with the action of the Board in view of the pending enquiries but having regard to the fact that the shareholders of the transferor company are stranded since the year 2003 and the shares that are offered for sale are a very small percentage of the total paid up capital, we are inclined to interfere and direct the Board to proceed with the letter of offer in accordance with law. Since the shares have not been listed, they cannot be traded in the market and the shareholders who are investors are stuck with those shares. Unless they are allowed to trade they will not get an option to exit if they want to. It is true that the shares which are now being offered for sale belong to Himachal which is under the scan of the Board but we cannot lose sight of the fact that as and when the shares are sold and the money is received, the Board will have ample powers under the Act to regulate and control the said amount. Himachal could also be directed to deposit the money with the Board. If the letter of offer is allowed to be withheld till the disposal of the proceedings under Section 11B, we do not know how long the shareholders will have to wait till they get an option to exit and their interest to that extent may suffer.

Proceedings in the enquiry have been stayed by the Delhi High Court and even though the learned senior counsel for the Board informs us that the writ petition is coming up for hearing next month, it will still take some time. After the petition is disposed of and, assuming the enquiry by the Board is to continue, that too, will take a long time as large number of entities are involved. Shareholders have been waiting since March 2003. Moreover, the appellant and Himachal have yet to be found guilty of the charges levelled against them. This apart, only 1.33% of the total paid up share capital is being offered for sale which is a small percentage of the shareholding and, as already observed, having regard to the interest of the public shareholders we direct the Board to proceed with the letter of offer and dispose of the same in accordance with law within six weeks from the date of receipt of a copy of this order.

5. There is yet another reason why we are directing the Board to proceed with the letter of offer. The Board has, in exercise to its powers under Section 11A of the Act, passed a general order laying down the procedure which it would follow in matters where offer documents are presented before it for consideration under the guidelines by entities who have been found violating some provisions of law and against whom an enquiry, adjudication, prosecution or other regulatory action is contemplated. It has also laid down the procedure for itself in cases where the entities who present the offer document are being proceeded against after the issuance of the show cause notice. In the case before us show cause notice had been issued against the appellant and Himachal when the letter of offer was presented to the Board. The general order of the Board in the case of such entities reads as under:

“2. Treatment where Show Cause Notice has been issued

Where a show cause notice has been issued to the entities, observations on draft offer document (s) filed by the issuer with the Board shall be kept in abeyance for a period of 90 days from the date of show cause notice or filing of draft offer document with the Board, whichever is later. The appropriate authority shall, in a fit case, within the period of 90 days, pass an appropriate interim or final order after hearing the person affected.

Provided that where there is any pending show cause notice as on the date of issuance of this General Order, the period of 90 days shall begin from the date of issuance of this General order.

Provided further that any time taken by such entities/noticee(s) shall be excluded while computing the 90 days period.

Where no such interim or final order is passed within the period of 90 days, the Board may process the draft offer document for the purpose of issuance of observations subject to relevant disclosures in the offer document about receipt of the show cause notice and the possible adverse impact of the order on the entities.

Issued by the Securities and Exchange Board of India by General Order dated 8th December 2006 in terms of power vested in it by S.11A (1)(b)”

The Board itself observes in this order that no person is presumed to be guilty unless proved to be so and, therefore, it would be in the interest of the investors and the securities market that their application for the consideration of offer documents be considered and disposed of within a reasonable period even when proceedings against such entities are contemplated or have been initiated. The guidelines framed by the Board provide that the offer documents are to be disposed of within a period of 21 days but in the case of entities against whom proceedings are either contemplated or have been initiated, the same shall be disposed of within a period of 90 days. This period has long expired and no action has been taken. There is logic in what the Board has said in the general order. In the case of offer documents presented by entities against whom any regulatory action is contemplated or to whom

show cause notices have been issued, the Board insists that they should make all relevant disclosures in the offer document including the receipt of show cause notice and the possible adverse impact it could have so that the investing public is adequately informed. The purpose of these disclosures is to enable the investing public to make informed investment decisions. It follows and the Board is aware that in the case of such entities, the consideration of the offer document is not to be withheld till the disposal of the proceedings against them but relevant disclosures are to be insisted upon. In the case in hand, the Board should and, we have no doubt that it shall, insist for such disclosures and leave it to the public to invest or not. Whoever then invests shall do so with eyes open and will have no cause to complain later. The guidelines also provide for such disclosures. This is in accordance with the scheme of the Act, different regulations and guidelines framed thereunder. The Board as a regulator has a duty to protect the interest of the investors and to promote the development of and to regulate the securities market by such measures as it thinks fit. It thought fit in its wisdom to issue the general order which, in our opinion, is in the interest of investors and the securities market and there is a recital to this effect in that order. In view of the general order passed by the Board, it should have itself disposed of the letter of offer as per the procedure stated therein.

6. During the course of the arguments, Shri J.J. Bhatt, learned senior counsel for the respondent stated that the condition imposed on Infotel by BSE was to divest its promoters' shares to the extent of 1.33%. BSE does not insist that Himachal alone should divest the shares. He argued that some other promoter(s) of Infotel could dilute the promoters' quota. The argument is quite attractive and we were inclined to accept the same but this is not possible

because the only promoter of Infotel is Himachal which holds 61.98% of its shares. The learned counsel for the appellant has placed before us the shareholding pattern of Infotel which is not disputed on behalf of the Board. It is clear therefrom that Himachal is the only promoter of Infotel. Since there is no other promoter of Infotel, the suggestion made on behalf of the Board cannot be accepted.

7. For the reasons recorded above, we allow the appeal, set aside the impugned order dated March 7, 2007 and direct the Board to proceed with the letter of offer presented by the appellant in accordance with law and issue a letter of observations in terms of the guidelines within six weeks from the date of receipt of a copy of this order. The Board should insist for strict compliance of the guidelines.

Before parting, we may notice a prayer made by the learned senior counsel on behalf of the respondent. He states that we should stay the operation of our order for a period of four weeks to enable the respondent Board to file an appeal in the Supreme Court. We do not think it is necessary for us to stay the operation because we have directed the Board to issue the letter of observations within six weeks and during this period it will have ample time to move the Apex court, if it so desires. No costs.

**Sd/-
Justice N.K. Sodhi
Presiding Officer**

**Sd/-
Arun Bhargava
Member**

**Sd/-
Utpal Bhattacharya
Member**

