

BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No. 60 of 2008

Date of decision: 15.10.2008

Mega Corporation Ltd. Appellant

Versus

Securities and Exchange Board of India Respondent

Mr. Jagdish Khanna Chartered Accountant for the Appellant.

Dr. Poornima Advani Advocate with Ms. Sejal Shah Advocate for the Respondent

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

Per : Utpal Bhattacharya, Member

This appeal has been filed under section 15T of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as the Act) against the order dated 28.2.2008 passed by the whole time member, Securities and Exchange Board of India (the Board for short) which, inter alia, restrains the appellant from accessing the capital market in any manner whatsoever for a period of one year for violation of regulations 3(a),(b),(c)&(d) and 4(1),4(2)(k) & 4(2)(r) of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (FUTP Regulations, for short). The restraint order was first passed as an ad interim ex parte order by the Board on 24.10.2005 which was confirmed on 24.7.2006 and was in force till the final order was passed on 28.2.2008. The sequence of events leading to the passing of the impugned order by the Board started off with an investigation conducted by the Board into the unusual price movements of the scrip of Mega Corporation Ltd., the appellant company, during the period from 25.1.2005 to 16.9.2005. Based on the findings in the investigation, the Board charged the appellant with manipulating the market in its own shares by several means. According to the show cause notice dated 10.10.2007 issued by the Board, a group of persons connected with the appellant indulged in a

large number of trades among themselves only to generate large trading volumes which resulted in raising the price of the scrip from Rs. 4.25 on 25.1.2005 to Rs.43.85 on 16.9.2005. The show cause notice further alleged that the appellant sought to generate investor interest in its scrip by publishing false and misleading announcements in the press about the company's prospects and business plans which projected unduly high revenues and profits for the company. It was also alleged that the company reported a huge profit in their annual results for the year 2004-05 by manipulating their books of accounts to induce the investors to buy the shares of the company.

2. Regarding the charge of manipulation of the scrip of the appellant company, it has been alleged that there was a sudden spurt in the volume of trading immediately after the results of the company for the quarter ending December 31, 2004 were announced. The learned representative of the appellant produced before us a copy of the results of the company for the quarter ended December 31, 2004 which showed miniscule amount of profit of Rs. 1.67 lacs against the comparable figure of 1.57 lacs of loss for the corresponding quarter of the previous year. We are satisfied that this kind of result cannot make any marked difference to the trading in the scrip of the company. Moreover, the small amount of profit was primarily a result of lower provision for depreciation which was done strictly in accordance with the correct accounting practices.

3. A more direct and more serious allegation regarding manipulation in the company's scrip is that a few traders, who were connected with the appellant company, purchased more than 2 crore shares in physical form on 5.3.2005 in off market deals and then transferred those shares in subsequent off market deals to certain other entities who were also alleged to be connected with the appellant company. The respondent Board has very painstakingly prepared an annexure to the show cause notice marked Annexure VII which shows the alleged connection among the entities who dealt heavily in the appellant company's scrip. The appellant company has totally denied any connection between it and those who traded in the scrip. We have perused this annexure and it does not indicate any link between any

of these traders and the appellant company. Annexure VIII to the show cause notice gives details of purchase of the appellant company's scrip by certain individuals and the onward transfer of the purchased shares to other entities in off market deals. In this annexure also, no link has been shown between any of these entities and the appellant company. The only connection between the trading entities and the appellant company that was persistently emphasised by the learned counsel for the respondent Board was firstly that three traders namely Patric Xess, Bahadur Singh and Deepak Sharma, who initially purchased large number of shares in off market deals and transferred those to others, were members of the appellant company and were present in the annual general meeting of the company held on 29.7.2005. The second link was that four of the traders namely Patric Xess, Nirmal Jain, Laxman Saijari and Mahendra Gopal Gorivale had the same address as that of Crayons Advertising Limited, an associate company of the appellant. As regards the second link, the learned representative of the appellant stated that Crayons Advertising Ltd. was not an associate company of the appellant but an associate company of another company controlled by one of the promoters of the appellant company. He also argued that the address given by the said four individuals was of a large building which had many offices located therein and there was no material at all to connect these individuals to any particular company. Last but not the least, he pointed out that the promoters of the appellant company did not sell any of their shareholding except for 3 lac shares in one block on 24.3.2005 at a price of Rs.14 each and so never derived any profit out of the increase in the price of its shares. What is stated by the learned representative of the appellant could not be controverted on behalf of the Board. After considering the rival contentions of the parties, we are of the view that the mere presence of any member of a company in its annual general meeting is not enough to establish a connection between the company and the member that can lead to a conclusion that the member would indulge in large scale fictitious trades on behalf of the company. There is no evidence in support of any definite sustainable link between the appellant company and any of the traders who allegedly traded in the appellant company's scrip with the purpose of generating volumes and thereby

raising its price. The charge of manipulative trading in its own shares by the appellant company, therefore, fails.

4. We shall now deal with the next charge in the show cause notice which is that the appellant, by publishing false and misleading announcements in the press regarding the company's future business prospects, attempted to generate investor interest in its scrip with the objective of boosting up its price and thereby violated regulations 4(2)(k) and 4(2)(r) of the FUTP Regulations. The learned counsel for the respondent Board relied upon two specific press announcements in order to make good this allegation. The first announcement made by the appellant company was dated 7.4.2005 which informed the general public that the appellant company proposed to launch "worldwide outbound package tour services" covering all the regions of the world. It intended to operate across 25 cities in India and expected to achieve a revenue of Rs. 1000 million in the first year with a net profit of Rs. 200 million. This announcement, according to the respondent Board, was "mischievously misleading and done with the sole purpose of generating interest in the scrip in the market". The second announcement was dated 20.4.2005 in which the appellant company announced that it was entering the business of foreign exchange with the launch of "Mega Forex" brand and that the company had applied to the Reserve Bank of India for the licence to deal in foreign exchange. It was also stated in the announcement that the company expected to grab 5-10 per cent of the market share in the forex market, "which is at \$ 5-6 billion" in "1-2 year time span". The case of the respondent Board is that this was a patently false announcement in as much as no application for licence had been made to the Reserve Bank of India till September 2005. Regarding the announcement made on tour business, we find that the business plan of the company for tour services was based on their agreement with the well known company Gem Tours and Travels Pvt. Ltd that had offices across the world. The original agreement between the appellant company and Gem Tours and Travels Pvt. Ltd. was produced before us so also the documents to establish that a subsidiary company called Mega Holidays Ltd. had been formed in order to handle the tour services business. The bank statement supports the payment of Rs. 15 lacs made to Gem Tours and Travels Pvt. Ltd on 11.4.2005 as a deposit in pursuance of the

agreement entered into with that company. As regards the second announcement pertaining to the launch of Mega Forex, it is clear that the application for licence to deal in foreign exchange made in September 2005 was only a revised application submitted by the appellant in response to the queries raised earlier by the Reserve Bank of India on their original application of 14.4.2005. The original application as well as the response of the Reserve Bank of India was produced for our perusal. After considering the submissions made by both sides and having examined the records, we are of the view that the information contained in the announcements was of a price sensitive nature which the appellant was obliged to make available to the stock exchange in terms of the listing agreement and so, there was nothing intrinsically wrong about their being published. Moreover, when the appellant company was proposing to start a new business venture, it is natural that it would give wide publicity to the same with a view to attract customers. Such publicity/advertisements cannot lead us to the inference that they were directed at investors rather than customers. We also find that the appellant had taken substantial steps necessary to implement the business proposals that were announced. May be, as contended by the learned representative of the appellant, the business proposals could not take off because of the exparte restraint order dated 24.10.2005 passed against the company. There is, thus, no reason to hold that the announcements were made only to mislead and dupe investors without any intention to implement them.

5. The third and last charge against the appellant is that it manipulated the accounts for the year 2004-05 to show inflated profits with a view to luring investors to buy shares of the company. The company had made losses for several years till it came out with a net profit of Rs. 9.24 crores for the year 2004-05. The profit was entirely attributable to the appellant company's income from trading in the shares of three companies, namely, Karuna Cables Ltd, Lakshmi Overseas Ltd and IFSL Ltd. These shares were sold in March 2005 after being purchased earlier during the same financial year. It is the Board's case that the transactions in these shares never took place and the profit was entirely fictitious. The evidence in support of this allegation is the finding by the Bombay Stock Exchange (BSE) that the trades did not take place on the online trading system of the exchange. It was also alleged by Shri Dinesh

Masalia, a director of DPS Shares and Securities Pvt. Ltd. (DPS), the appellant's broker that the contract notes issued to the appellant were not genuine. Even the appellant's demat account, which was produced before this tribunal, did not show any transaction in any of the three scrips, whether on the exchange or off market. Yet another piece of evidence brought forth by the Board is that though the appellant held more than 1 per cent of the share capital of Karuna Cables Ltd, Lakshmi Overseas Ltd and IFSL Ltd., none of them showed the name of the appellant in the list of their shareholders holding more than 1 per cent shares. All these pieces of evidence, taken together, make it appear that the transactions did not actually take place. The appellant, however, took the stand that it had dealt only with its broker who alone would be in a position to clarify the points raised by the Board. It is the case of the appellant that it had placed orders for sale and purchase of shares with DPS and the latter alone would know how the trades were executed. Shri Dinesh Masalia, a director of DPS complained to the Board that the broker had not handled the appellant's trades in the three aforesaid scrips and that the contract notes issued to the appellant were forged. The Board has relied upon this statement to hold that the trades were fictitious. We have on record at least two cheques of Rs.20 lacs each signed by Shri Dinesh Masalia on behalf of DPS which were issued to the appellant towards payment of the latter's dues on the sale of scrips. In view of this documentary evidence, the statement of Shri Masalia has to be taken with the pinch of salt. This apart, when the appellant came to know of the statement made by Shri Dinesh Masalia, the former immediately demanded cross-examination of the latter which was denied by the Board. Since the appellant and Shri Masalia had taken diametrically opposite stand, it was a fit case where the appellant should have been allowed to cross-examine Shri Dinesh Masalia. Not having been allowed to do so, we are clearly of the view that the principles of natural justice stood violated. The Board was also in error in relying upon the statement of Shri Dinesh Masalia. It is true that the broker alone would know and would be responsible for the nature of the trades that it carried out on behalf of the appellant, but we cannot loose sight of the fact that the sale proceeds of the shares amounting to more than Rs.10 crore had actually been received by the appellant and this fact remains uncontroverted.

6. The question we are primarily concerned with is not whether the annual accounts of the appellants for the year 2004-05 were correctly drawn up or had shown inflated profit. In fact that is not even the primary concern of the Board in as much as in its ad interim ex parte order dated 24.10.2005, the whole time member of the Board mentioned that a reference was being made to the Institute of Chartered Accountants of India to examine the role of the auditor in certifying the annual accounts of the appellant. Our primary concern in the matter is whether through the annual accounts, the investors in the market were led to believe that the appellant's performance was excellent and that its shares were worth investing in. Normally, whenever any company comes out with positive annual results that are substantially better than the results of the previous few years, there will be a positive response among the investors. But it is another matter to say that a company has manipulated its accounts with that specific object in view because there can be a multitude of reasons why an unscrupulous management may want to show inflated financial results in its accounts. In the present case, no material has been produced by the respondent to establish that the manipulation in the annual accounts of the appellant for the year 2004-05, if any, had been resorted to with the objective of luring investors to buy the scrip of the company. Given the lack of any definite evidence, this charge against the appellant also fails.

7. Before concluding, we would like to mention that there are statements made by several persons which are available on the records of this case and which have been stoutly denied by the appellant. These include the statements of two directors of the appellant's broker DPS to the effect that the purchase and sale of shares executed by DPS on behalf of the appellant company were completely false and fabricated and that payments were made to the appellant company on account of such dummy sales out of the funds provided by the appellant company itself. There is also a letter addressed to the respondent Board by one Sanjeev Kathuria alleging the involvement of one of the directors of the appellant company in manipulative trading in its shares. The learned representative of the appellant company, apart from denying the allegations, demanded cross examination of the persons and because such cross examination was not allowed, these statements could not be relied upon by the

respondent. Considering that the respondent Board undertook a process of enquiry under section 11B of the Act which is quasi judicial in nature, we do not see any reason for the Board to shy away from allowing cross examination. In a situation where one person's assertion is being directly contradicted by another, what could be a better way of arriving at the truth of the matter which is the only aim of an enquiry? Obviously, enquiries need not and should not be limited to examination of documents alone relying on statements recorded at the time of investigation. We trust that the respondent Board will take note of this position and allow examination as well as cross examination of witnesses during the process of enquiry, wherever necessary, whether by an enquiry officer or by a whole time member or by an adjudicating officer under chapter VIA of the Act.

8. To sum up, the main charge of manipulative trading in its own shares by the appellant fails in the absence of any link being established by the respondent Board between any of the traders with the appellant company. The charge of making false and misleading announcements as also that of manipulation in the annual accounts of 2004-05 in order to lure investors also does not succeed. We have, therefore, no hesitation in allowing the appeal and setting aside the impugned order. No order as to costs.

Sd/-
Justice N.K. Sodhi
Presiding Officer

Sd/-
Arun Bhargava
Member

Sd/-
Utpal Bhattacharya
Member

15.10.2008
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