BEFORE THE SECURITIES APPELLATE TRIBUNAL MUMBAI

Appeal No. 90 of 2007

Date of decision : 20.11.2008

Dilip S. Pendse …… Appellant

Versus

Securities and Exchange Board of India …… Respondent

Mr. V.M. Singh Advocate for the Appellant.

Mr. Kumar Desai Advocate with Ms. Daya Gupta Advocate for the Respondent

Coram : Justice N.K. Sodhi, Presiding Officer
Utpal Bhattacharya, Member

Per : Justice N.K. Sodhi, Presiding Officer

Tata Finance Limited (hereinafter called TFL) is a public limited company belonging to the Tata group and its shares are listed on the Bombay Stock Exchange (BSE) and the National Stock Exchange of India Limited (NSE). Niskalp Investments and Trading Company Limited (for short Niskalp) is an investment company and a wholly owned subsidiary of TFL. Shri Dilip S. Pendse (Pendse) who is the appellant before us was the managing director of TFL from 1.6.1996 to 31.5.2001 and a director of Niskalp during the period from 19.6.1997 to 1.6.2001. One Shri Jaivant Esvonta Talaulicar (Talaulicar) was a director of TFL from January, 1995 to August, 2001 and also a director of Niskalp from March 15, 1991 and its chairman from May, 1995 till September 21, 2001. The Securities and Exchange Board of India (for short the Board) conducted investigations during August/November, 2001 into the alleged manipulation and insider trading in the shares of TFL. Investigations prima facie revealed that Pendse aided Talaulicar through counselling and organized deals on his behalf in the shares of TFL and thereby indulged in insider trading violating Regulation 3 of the Securities and Exchange Board of India (Insider Trading) Regulations, 1992 (for short the Regulations). The Board decided to initiate adjudication proceedings against Pendse. Accordingly, a show cause notice dated

September 29, 2003 was issued calling upon him to show cause why penalty be not imposed on him in terms of section 15G of the Securities and Exchange Board of India Act, 1992 read with Regulation 4 of the Regulations for violating Regulation 3. The allegations in the show cause notice are that Talaulicar and his family members sold on 30.3.2001, one lac shares of TFL at a negotiated price of Rs.69 per share to JIP Investment (JIP) which is a sub-broker of JHP Securities Private Limited (JHP) which in turn is a broker member of BSE. This was an off market transaction and the shares were purchased by JIP in its proprietary account. On the following day (31.3.2001), JIP issued five cheques totalling Rs.69 lacs to Talaulicar. These cheques were encashed between 4.4.2001 and 7.4.2001 and Talaulicar issued delivery instructions on 4.4.2001 transferring the shares in the name of JIP. The Board has also found that on 30.3.2001 JIP received Rs.69 lacs from JHP and JHP had received Rs.70 lacs from Niskalp. This is one part of the story. It is also the case of the Board that JIP then sold one lac shares on behalf of Talaulicar through the exchange through JHP and one Bharat Patel (brokers) at the then prevailing market price. These shares were sold between 18th and 29th May, 2001 at an average price of Rs.35 per share and JIP received in all Rs.34.21 lacs. This amount is far less than the amount which JIP paid to Talaulicar when the latter sold the shares on 30.3.2001. Talaluicar then paid a sum of Rs.34.79 lacs (the difference between the price at which Talaulicar sold the shares to JIP and the price at which the JIP sold the shares in the market). JIP paid this amount to JHP which in turn paid to Niskalp. Pendse, the appellant herein does not figure anywhere when we look at the transactions both in regard to the transfer of shares and the receipt of money by different entities.

2. TFL had come out with a rights issue that opened on 30.3.2001 and closed on 30.4.2001. Niskalp which is a subsidiary of TFL had then suffered huge losses which fact was not disclosed to the shareholders in the letter of offer that was issued on behalf of TFL and when this non-disclosure was discovered, the shareholders were given an option to withdraw their subscription and not to participate in the rights issue. What is alleged by the Board is that both Pendse and Talaulicar being the directors of TFL and Niskalp were ‘insiders’ within the meaning of Regulation 2(e) of the Regulations who knew about the losses suffered by Niskalp which was unpublished price sensitive information and they

deliberately withheld the same from the shareholders. Before this price sensitive information could be made public, Talaulicar sold his shares at an exorbitantly high price in the aforesaid manner thereby violating Regulation 3 of the Regulations which at the relevant time prohibited an insider from trading in securities of a company listed on any stock exchange on the basis of any unpublished price sensitive information. Talaulicar has been proceeded against and by a separate order monetary penalty has been levied on him. He has filed Appeal no. 23 of 2007 which is pending before this Tribunal and we are informed that he has moved an application for a consent order which is pending before the Board. We are not concerned with that Appeal in this case. However, Talaulicar was examined and he appeared during the course of the investigations and his statement was recorded on 18.6.2002. He was specifically asked as to why he transferred his family shares in TFL to JIP on April 4, 2001 and his reply was as under:

> "As already set out in my written representation dated 30th November, 2001 I required funds for the purchase of a retiral residence at Goa. At the instance and recommendation of Mr. Pendse I applied for a loan from Tata Home Finance Ltd. (THFL). Section 295 of the Companies Act, 1956 permission was required for this loan. I made a loan application to THFL on 25.09.2000. THFL, in turn, pursued the Section 295 sanction from the appropriate authority from September 2000 onwards. The Section 295 sanction was overseen by Mr. Pendse. In March 2001 Mr. Pendse informed me that the Section 295 sanction was unlikely to come through. As the THFL loan application which was for Rs.75.00 lacs was unlikely to go through and as I required funds for my Goa residence from my investments, I requested Mr. Pendse to sell my family's 1.00 lacs shares. In consideration for my shares he handed over cheques of the aggregate consideration of Rs.69.00 lacs and I executed delivery instructions to my Depository namely HSBC. Mr. Pendse had told me that the sale of the said shares was to a friend of his. I did not know to whom the shares were sold or when exactly they were sold/transferred. This is borne out by my letter August 30, 2001 addressed to HSBC requesting information with regard to the exact date of transfer, no. of shares transferred and to the account to which the shares were transferred. I only learnt on 27.10.2001 that the shares had been transferred to JIP's Demat Account with Mafatlal Securities on April 04, 2001. "

He was also asked as to whether he insisted for the contract notes to be issued for the sale transactions and he replied as under:

> "Yes. I repeatedly followed up the matter with Mr. Pendse and Mr. Shilotri for the sale contracts and they informed that the shares were purchased by a friend of theirs and that they

> would give the contract notes soon. When I contacted Mr. Pendse and Mr. Shilotri in May, 2001, they represented to me that the shares infact had not been sold and that they would organise the sale now."

On the basis of the stand taken by Talaulicar, the Board was of the view that Pendse had aided him by way of counseling and organized the transfer of shares on his behalf in the manner stated hereinabove and thereby Pendse was guilty of insider trading and he, too, violated Regulation 3 of the Regulations. Hence the show cause notice to Pendse referred to above. A copy of the statement made by Talaulicar was also furnished to him. Pendse filed his detailed reply to the show cause notice denying the allegations made against him. He denied having committed any offence as alleged in the notice and specifically pleaded that he was not involved in any of the transactions referred to in the show cause notice and he had no concern with the transfer of shares or receipt of money by the entities. He also took a stand that he dissuaded Talaulicar from selling the shares. He has denied any knowledge regarding the payment of Rs.69 lacs by JIP to Talaulicar and also regarding the transfer of shares by Talaulicar to JIP on 4.4.2001. He has denied that he organized any trade(s) on behalf of Talaulicar. Since the appellant was being roped in on the statement of Talaulicar whom he described as the primary wrong doer, he pleaded that no credence be given to the uncorroborated testimony of Talaulicar and that he wanted to cross-examine him (Talaulicar).

3. On a consideration of the material collected during the course of investigations and having examined the record in regard to the various transactions by which the shares were transferred by Talaulicar to JIP and subsequent transfers as well and relying on the statement of Talaulicar, the adjudicating officer came to the conclusion that the charge of aiding and organizing trades on behalf of Talaulicar stood established against the appellant. After taking into consideration the factors enumerated in Section 15 J of the Act, the adjudicating officer by his order dated December 29, 2006 imposed a monetary penalty of Rs.1,50,000/- on Pendse. It is against this order that the present appeal has been filed.

4. We have heard the learned counsel for the parties at length and have also examined very carefully the records of the case including the impugned order. The learned counsel

for the appellant absolutely denied any involvement whatsoever of his client with the sale of TFL shares by Talaulicar in any manner. He challenged the correctness of the statement of Talaulicar and contended that the adjudicating officer was not justified in relying on that statement without allowing the appellant to cross examine him. In the impugned order, the only evidence referred to of Pendse's involvement in Talaulicar's sale of TFL shares is the statement of Talaulicar which is on record.

5. In paragraph 3.9.2 of the impugned order, the adjudicating officer has observed that Pendse had admittedly advised Talaulicar to take a loan for acquiring a flat in Goa rather than sell his family's TFL shares. From this he concludes, apparently without a shred of evidence, that when Talaulicar's housing loan application did not succeed, Pendse must have "assisted or guided or aided" Talaulicar in the sale of one lac shares of TFL. There is absolutely no evidence whatsoever for the conclusion drawn by the adjudicating officer that it was Pendse who handed over cheques for Rs.69 lacs to Talaulicar as consideration for the supposed sale of one lac TFL shares. It has been noted in paragraph 2.1 (j) of the impugned order that "Shri Pendse had contacted Shri Bharat Patel around 27.3.2001 to undertake two back dated sale and purchase transactions in TFL shares at a price around 69-70 per share." Bharat Patel was a broker through whom Talaulicar's shares were sold in May 2001 and there is no confirmation of this in his statement recorded during the course of investigations. In fact, in his statement dated 17.4.2002, Shri Bharat Patel has categorically denied that anybody ever approached him for arranging any finance for Talaulicar and/or his family.

6. In paragraph 3.9.3 of the impugned order it has been observed that "the sale had been organised by Shri Pendse through an off market deal". Apart from the statement made by Talaulicar, there is not an iota of evidence to corroborate this observation/finding. The adjudicating officer has taken considerable pains to establish that Pendse was an insider as far as TFL and Niskalp were concerned and having done that, he jumps to the conclusion that Pendse must have counselled and aided Talaulicar in the alleged insider trading of one lac TFL shares. He forgets that Talaulicar himself was an insider and did not require any counselling or aiding. In whatever manner one analyses the impugned

order, ultimately Pendse's culpability has been inferred essentially on the basis of Talaulicar's statement.

7. This brings us to the core issue whether Pendse was guilty of insider trading by counselling and aiding Talaulicar in transferring his TFL shares. The details of the reply to the show cause notice given by the appellant have been meticulously noted in the impugned order except the plea made by the appellant to allow him to cross examine Talaulicar on whose statement the whole case hinges. This plea, as already mentioned, has not even been noticed by the adjudicating officer not to speak of allowing the appellant an opportunity to cross examine Talaulicar. During the hearing, the learned counsel for the respondent Board argued that cross examination was not allowed because the appellant did not specifically ask for the same during the hearing before the adjudicating officer and, therefore, there was no violation of the principles of natural justice in that respect. This is a specious argument. What the adjudicating officer has done, in effect, is to entirely rely on the statement of Talaulicar practically without there being any corroboration from anywhere else. The statement of Talaulicar has been strongly refuted by Pendse and the latter contends that he played no role whatsoever in the sale of shares of TFL by Talaulicar. This is a case where we have the word of Talaulicar against that of Pendse and in the absence of any corroboration, the only way out was to allow Pendse to cross examine Talaulicar. Not having done so, the principles of natural justice have been violated. The cross examination of Talaulicar, if allowed, would have given the appellant the opportunity of specifically contradicting and proving wrong Talaulicar's statement and in the absence of such an opportunity it is far from correct to hold that the principles of natural justice have not been violated. In this view of the matter, the charge of insider trading cannot be said to have been established against Pendse. We have been noticing the same kind of unwillingness on the part of the respondent Board in similar circumstances to permit cross examination of parties by the opposite side during enquiries conducted by it. We consider it necessary to remind the respondent Board once again that in a situation where one person's statement is being relied upon as against the other, permitting cross examination of that person by the opposing side is the best way of arriving at the truth which is the only aim of an enquiry, whether the enquiry is by a whole time member or by

an enquiry officer or by an adjudicating officer. We hope that this fundamental principle is not lost sight of by the respondent Board.

8. Apart from what has been stated above, the adjudicating officer seems to have relied, to some extent, upon the findings of some committee set up by the Tata Group to go into the dealings in TFL shares by Pendse and others. The appellant has categorically stated in his reply to the show cause notice that he had not been associated in any manner with the said investigations and enquiries carried out by the committee constituted by the Tata Group. Even otherwise, the findings and the conclusions arrived at by a private body cannot be cited, much less relied upon, by the adjudicating officer in quasi judicial proceedings. Every finding of the adjudicating officer must be based on an independent appraisal of the evidence on record and cannot be allowed to be influenced by extraneous factors. For the same reason we do not appreciate the adjudicating officer's reference to the appellant being penalised for the same alleged mischief in an enquiry under section 11 of the Act and Pendse's appeal against that order being dismissed by this Tribunal. We would like to point out that Pendse's Appeal no.92 of 2005 against that order was not dismissed by this Tribunal on merits but only because the period of penalty had already been suffered by Pendse and the appeal had become infructuous.

9. If it had been only the question of Pendse not being allowed to cross examine Talaulicar in the adjudication proceedings, we would have decided to remit the case back to the adjudicating officer for re-enquiry. But the entire case of insider trading on the part of Pendse as made out by the Board suffers from lack of credibility. Talaulicar was a senior professional manager in the investment market heading Niskalp, an investment and trading company, as its chairman. Pendse, who was the managing director of TFL, was also similarly placed on the professional front. As far as TFL and Niskalp were concerned, both Pendse and Talaulicar were admittedly insiders. If Talaulicar wanted to sell a large number of his shares in TFL, he would know how to sell, when to sell and who would be the likely purchasers. There should not have been any occasion for him to seek Pendse's assistance and if such a conclusion is drawn, as has been done by the adjudicating officer, there has to be clear evidence to support such a conclusion which is conspicuous by its

absence in this case. A part of the allegation levelled by the Board is that before Talaulicar received Rs.69 lacs from the broker as the purported sale price for 1 lac shares of TFL, this amount had actually come out of the sum of Rs.70 lacs paid by Niskalp to the broker JHP. Assuming that the funds really flowed in this manner from Niskalp to JHP and then to Talaulicar via JIP, then rather than hold Pendse responsible for utilizing funds from Niskalp for the purpose, should Talaulicar, who was the chairman of Niskalp at that point of time, not be held responsible? Similarly, in his statement during investigations, Talaulicar has stated that it was Pendse who handed over cheques for the aggregate value of Rs.69 lacs to him for the sale of his family's shares. There is absolutely no corroboration in support of such a statement and a serious allegation like insider trading cannot be established on the basis of such uncorroborated evidence. Talaulicar was not an inexperienced person who would need his hands to be held when he decided to offload his TFL shares in the market. That Pendse counselled and aided Talaulicar in marketing the latter's TFL shares cannot be concluded on the basis of indirect and circumstantial evidence based on uncorroborated statements of persons like Talaulicar who might be trying to disown or dilute his own responsibility by shifting the blame to Pendse for insider trading. In this view of the matter, the case set up against Pendse does not inspire confidence and for this reason we are not remitting the case back to the adjudicating officer.

In the result, the appeal is allowed and the impugned order set aside. No order as to costs.

Sd/-
Justice N.K. Sodhi
Presiding Officer

Sd/-
Utpal Bhattacharya
Member

20.11.2008
pmb, ddg & rhn/-