WTM/RKA/ISD/ 14 /2014

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA
ORDER

UNDER SECTIONS 11(1), 11(4) and 11B OF THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 AND SECTION 12A OF THE SECURITIES CONTRACTS (REGULATION) ACT, 1956 - IN THE MATTER OF ZENITH INFOTECH LTD.

In respect of:

Sl. No.	Name of the entities	PAN/DIN
1	Mr. Rajkumar Saraf (Promoter and Chairman-cum-Director)	AURPS4374C
2	Mr. Akash Rajkumar Saraf (Promoter and Managing Director)	AAFPS8849C
3	Ms. Devita Rajkumar Saraf (Promoter)	AAFPS8848D
4	Ms. Vijayrani Rajkumar Saraf (Promoter)	AMTPS0851J
5	Zenith Technologies Pvt. Ltd. (Promoter)	AAACZ2074L
6	Vu Technologies Pvt. Ltd. (Promoter)	AACCV1663P
7	Mr. Vipin M. Shah (Director)	AAHPS8417J
8	Mr. Vijay Ramchandra Mukhi (Independent Director)	00002633

(hereinafter collectively referred to as "the noticees" or by their respective names.)

Appearances:

For noticees 1 to 6:
1. Mr. Ravi Kadam, Senior Advocate
2. Mr. KRCV Seshachalam, Advocate
3. Mr. Nirav Shah, Advocate
4. Mr. Rajkumar Saraf
5. Mr. Akash Rajkumar Saraf

For noticees 7 and 8: **None**

For SEBI:
1. Mr. Gyan Bhushan, Executive Director
2. Mr. Santosh Kumar Shukla, Joint Legal Adviser
3. Mr. Vijayakrishnan G., Deputy Legal Adviser
4. Mr. K. Saravanan, Deputy General Manager
5. Mr. Rakesh Singh, Assistant Legal Adviser
6. Mr. Parag K Sinha, Assistant Legal Adviser
7. Mr. Abhiraj Arora, Legal Officer

1. Vide an *ad interim ex-parte* order dated March 25, 2013 (hereinafter referred to as the *'interim order'*) SEBI *inter alia* restrained Mr. Rajkumar Saraf, Mr. Akash Rajkumar Saraf, Ms. Devita Rajkumar Saraf, Ms. Vijayrani Rajkumar Saraf, Zenith Technologies Pvt. Ltd. and Vu Technologies Pvt. Ltd. who are the persons belonging to the promoter group of Zenith Infotech Ltd. (hereinafter referred to as "ZIL" or "the company") from accessing the securities market and further prohibited them from buying, selling or dealing in securities, directly or indirectly, in any manner whatsoever, till further directions. Further, the board of directors of ZIL were directed to furnish, within 30 days from the date of the *interim order,* bank guarantee(s) of a minimum tenure of one year for USD 33.93 million in the name of SEBI without using the funds of ZIL or creating any charge on the assets of ZIL. As per the *interim order*, the bank guarantee was to be invoked should any adverse inference is drawn by SEBI in its final order with regard to the actions of the promoters/board of directors of ZIL in diverting the sale proceeds of Managed Services Division (MSD) of the company and SEBI deems it necessary to compensate ZIL.

2. The *interim order* was passed on the basis of *prima facie* findings that the noticees have acted in fraudulent and deceitful manner and contravened the provisions of the Securities and Exchange Board of India Act, 1992 (the SEBI Act), the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (the PFUTP Regulations), clauses 21 and 36 of the Equity Listing Agreement (listing agreement) read with section 21 of the Securities Contracts (Regulation) Act, 1956 (the SCRA), Code of Corporate Disclosure Practices for Prevention of Insider Trading provided in Schedule II of the Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992 (the PIT Regulations). By the *interim order,* the noticees were also provided 21 days time to file their replies to the allegations and also to avail opportunity of personal hearing, if they so desire.

3. The noticees no. 1 to 6 and ZIL preferred an appeal before the Hon'ble Securities Appellate Tribunal (SAT) impugning the said *interim order*. Some of the FCCB holders, namely, QVT Fund L.P. and Quintessence Fund L.P., who between themselves held 75.6% in the 2011 FCCBs and 57% in the 2012 FCCBs, also filed a miscellaneous application before the Hon'ble SAT to intervene in the matter which was subsequently allowed by the Hon'ble SAT. The Hon'ble SAT, vide order dated July 23, 2013 set aside the *interim order*.

4. This order of the Hon'ble SAT was challenged by SEBI in an appeal before the Hon'ble Supreme Court. On August 27, 2013, the Hon'ble Supreme Court issued notice, and stayed the operation of the order dated July 23, 2013 of the Hon'ble SAT. Some of the respondents in the said civil appeal (i.e. the appellants before the Hon'ble SAT) filed an interim application before the Hon'ble Supreme Court seeking modification in its order dated August 27, 2013. Vide its order dated September 10, 2013, the Hon'ble Supreme Court dismissed the said interim

application and extended the time period for furnishing the bank guarantee, as directed in the *interim order,* from 30 days to 40 days. On September 26, 2013, the Hon'ble Supreme Court refused the prayer of these respondents seeking further extension of the time and directed SEBI not to take any steps against ZIL for furnishing of the bank guarantee, till the next date fixed in the matter, i.e., October 24, 2103.

5. Mr. Rajkumar Saraf, Mr. Akash Rajkumar Saraf, Ms. Devita Rajkumar Saraf, Ms. Vijayrani Rajkumar Saraf, Mr. Vipin M. Shah, Zenith Technologies Pvt. Ltd., Vu Technologies Pvt. Ltd. and Mr. Vijay Ramchandra Mukhi filed their replies in response to the *interim order*, vide their letters dated January 28, 2014. An opportunity for personal hearing was granted to the noticees by SEBI on February 25, 2014, which was adjourned at the request of the noticees.

6. In the meantime, the above-stated FCCB holders filed an interim application before the Hon'ble Supreme Court seeking direction to the board of directors of ZIL to comply with order of the Hon'ble Supreme Court dated September 10, 2013, i.e. the direction to submit the bank guarantee within 40 days. The interim application was heard on March 03, 2014 when the Hon'ble Supreme Court directed SEBI to give a hearing to the board of directors of ZIL on March 06, 2014 with regard to the directions given in the *interim order* dated March 25, 2013 and listed the application for hearing on March 24, 2014.

7. As directed, SEBI granted an opportunity of personal hearing to the noticees on March 06, 2014 when their authorized representatives appeared and made submissions on their behalf. They also filed their written submissions vide their letter dated March 11, 2014.

8. The submissions of the noticees are *inter alia* as under:

   (a). Copy of the complaints which have been allegedly filed against ZIL and noticees as referred in the *interim order* have not been provided. Further, the principles of natural justice have not been observed while passing the *interim order* as no opportunity of being heard was provided before passing the *interim order* in this case. An *ad interim ex parte* order must necessarily be warranted by grounds of urgency and must be fair, reasonable and judicious. However, none of these ingredients are present in the *interim order*. The directions therein could be issued only after providing opportunity of being heard.

   (b). The *interim order* had been passed in the context of purported defaults committed by ZIL in repaying the FCCBs and purported deviation by ZIL of the shareholders' resolution to sell a division or subsidiary or assets, etc. purportedly to repay the FCCBs. SEBI lacks jurisdiction in respect of FCCBs which are administered by RBI.

   (c). The matters covered under the *interim order* are *sub judice* before the Hon'ble Bombay High Court in Civil Suit No. 2865 of 2011. The FCCB holders have also filed winding up petition (Company Petition no. 28 of 2012) against ZIL. The Hon'ble Bombay High Court has given adequate protection to the FCCB holders and SEBI need not interfere in the matter.

(d). As per section 55A of the Companies Act, 1956, SEBI's jurisdiction is limited to issue and transfer of securities and non-payment of dividend. FCCBs are not "securities" as defined under section 2(h) of the SCRA and hence not within the regulatory purview of SEBI. The issues alleged in the *interim order* are exclusively under the jurisdiction of the Ministry of Corporate Affairs (MCA). If there is a failure to comply with the shareholders resolution, the aggrieved shareholders have remedies available to them under the Companies Act, 1956 and SEBI has no jurisdiction to enforce shareholders resolution**.**

(e). As stated under frequently asked question (FAQ's) entitled "Investors Grievance Redressal Mechanism at SEBI" (dated November 26, 2011) it is SEBI's policy of not passing orders on matters which are *sub judice* before Civil Courts. In the said FAQ it is also stated that grievances pertaining to mismanagement of company, minority shareholders interest, etc. fall within the ambit of the MCA.

(f). The *interim order* is beyond jurisdiction, powers and functions of SEBI as available under the SEBI Act. Sections 11, 11(4), 11B and 12A of the SEBI Act and section 12A of the SCRA, which are used as source of power to pass the *interim order* do not include the matters specified in section 55A of the Companies Act.

(g). The power under section 11(4) of the SEBI Act is exhaustive and it does not include the power to direct the bank guarantee as directed in para 25(ii) of the *interim order*. The intent of bank guarantee is that in the event of any adverse finding if the Hon'ble Bombay High Court decides the case against the company, the SEBI will invoke the bank guarantee and that may be used for compensating the FCCB holders. Such direction cannot be issued under section 11(4)(d) of the SEBI Act that empowers SEBI to impound and retain the proceeds or securities in respect of any transaction which is under investigation. In this case, the proceeds or securities are not involved and SEBI does not seem to have initiated any investigation in the matter. Section 11(4)(f) of the SEBI Act empowers SEBI to direct a person associated with the securities market not to dispose of or alienate an asset forming part of any transaction which is under investigation but does not include the power to direct the bank guarantee as in the instant case. The power under section 11 (4)(d) and (f) of the SEBI Act with respect to a listed company is limited in the context of insider trading or fraudulent or unfair trade practices relating to securities market. Hence, section 11(4) of the SEBI Act does not apply on the facts of this case.

(h). The *interim order* could not have been passed under section 12A of the SCRA since an order under section 12A can only be passed against a stock exchange or clearing corporation or any other agency that provides clearing and settlement facilities in respect of securities.

(i). In the proceedings before the Hon'ble SAT, SEBI in its reply stated that it had invoked its jurisdiction because the Hon'ble Bombay High Court did not pass any orders providing the security to the FCCB holders. According to the noticees, the Hon'ble Bombay High Court vide its order dated October 09, 2012 in the recovery suit, has provided a security of almost

₹497 crores to the FCCB holders. Despite having the protection of the aforesaid order, SEBI erroneously passed the *interim order* under the garb of "investor protection".

(j). The effect of direction under para 25(ii) is in the nature of disgorgement and the *interim order* in this case is in aid of passing an order of disgorgement. The power under section 11B is very wide but it does not include the power of interim directions in the nature of interim disgorgement as sought to be done in this case. The disgorgement order can be passed only after coming to the final conclusion that the person against whom such order is passed has made profit or avoided loss. Relying upon order dated November 22, 2007 of the Hon'ble SAT in the matter of *National Securities Depository Limited vs SEBI* in Appeal no. 147 of 2006, it has been submitted that an order of disgorgement before conclusively proving that there are illegitimate gains or that there are avoidance of loss cannot be passed. This direction is in nature of mandatory injunction, attachment before judgment and monetary penalty.

(k). There is no allegation in the *interim order* that board of directors had acted *mala fide* or against the interest of ZIL or that they gained unlawfully or that they avoided loss.

(l). In other matters, where SEBI has issued *ad-interim ex-parte* orders under section 11 of the SEBI Act against defaulting companies in relation to diversion of monies received *via* Initial Public Offerings ("IPO"), no orders have been issued by SEBI directing the promoters/directors of such companies to furnish any personal guarantee or personally bring back the purported diverted IPO funds. In this regard, the noticees have placed reliance on the orders passed by SEBI against certain companies on December 28, 2011.

(m). The commissions/omissions alleged in the *interim order* do not attract definition of "fraud" under the regulation 2(1)(c) of the PFUTP Regulations, since the entire edifice of the said regulations stands on the footing "while dealing in securities".

(n). Section 12A of the SEBI Act and regulations 3(c) and (d) of the PFUTP Regulations cannot be invoked in the present proceedings for the reason that there was no allegation/charge in the order that noticees have dealt in securities to attract this provision. Further, there is no allegation in the *interim order* that the noticees have employed any artifice or scheme to defraud in connection with "dealing in" or "issue of securities" which are listed or proposed to be listed on any stock exchange. Further, as the FCCBs are not securities listed or proposed to be listed on any recognised stock exchange, the charge of violation of these provisions cannot sustain. The words *'in connection with'* in section 12A of the SEBI Act are of wide import but the section cannot be read to extend it to securities which are neither listed nor proposed to be listed. The intention of section 12A is that the concerned device, scheme or artifice to defraud must be in connection with and in regard to dealing in the securities that are listed or proposed to be listed.

(o). Clause 21 of the listing agreement does not apply to FCCBs. The noticees have complied with the requirements of Clause 36 of the listing agreement and Clauses 2.1, and 7.0 (ii) of Code Of Corporate Disclosure Practices For Prevention Of Insider Trading provided in Schedule II read with Regulation 12 (2) of the PIT Regulations and this is apparent from the

BSE announcements dated September 26, 2011 and October 13, 2011. There was no default in disclosing the default of FCCBs to the exchanges, though there was a delay in disclosing to exchanges since the noticees were in negotiations with the concerned FCCB holders for rescheduling and repayment.

(p). The allegation that the announcement dated December 27, 2010 was made as a promise without intending to perform is denied. It is submitted that the two resolutions proposed in the notice of the Extraordinary General Meeting (EGM) to be held on January 29, 2011 were not only for the purpose of redemption of FCCBs as alleged in the *interim order* but were general and inclusive to include other purposes also.

(q). The *interim order* is based on assertion of an alleged diversion of funds which is factually incorrect. When sale proceeds of MSD business was realized, the same could not have been used for redemption of FCCBs as the trustee-representative of the FCCB holders refused to accept these monies. Trustees insisted that the default of 2011 FCCBs had triggered the cross default in 2012 FCCBs and hence payment under both the 2011 FCCBs and 2012 FCCBs were to be paid immediately in full. ZIL could not have repaid the 2012 FCCB holders as they would have had to seek prior RBI approval for pre-payment of a foreign loan. It is in these circumstances, the payments made out of MSD business, now being characterized as diversion, were made after October 10, 2011 when the negotiations had failed.

(r). There has been no siphoning off/asset stripping of assets of ZIL by the noticees as alleged in the *interim order*, since ZIL and its wholly owned subsidiaries were the direct beneficiaries of the funds obtained through sale of MSD business and hence ZIL can only be the party which can bring back the funds. The entire sale proceeds of the MSD business have been utilized for the legitimate business purposes such as the payment of taxes, loans, secure creditors, trade creditors, etc. Out of the alleged diversion of USD 33.93 million, the fund transfers amounting to USD 10.4 million to Zenith Singapore, a subsidiary of ZIL, was made by ZIL and Zenith Dubai so as to enable Zenith Singapore to repay the working capital limit availed from Standard Chartered Bank (SCB) Singapore by Zenith Singapore. Further, USD 10.53 million was utilized to make payment to other business creditors and for the purchase of capital goods. The remaining amount of USD 13 million (approximately) was invested in Cloud Dubai and VU Dubai.

(s). ZIL's accounts for the financial period ending September 30, 2011 and September 30, 2012 were adopted by the shareholders in successive annual general meetings of ZIL held on February 4, 2012 and March 28, 2013. By a resolution passed by the shareholders in the Annual General Meeting held on March 28, 2013 the shareholders of ZIL have ratified the manner in which the sale proceeds of MSD business have been disbursed for the financial period ending September 30, 2012.

(t). The fall in share prices of ZIL cannot be attributed to the noticees' actions or inactions.

(u). On October 12, 2011, the day before ZIL informed stock exchanges that it had defaulted on redemption of FCCBs, the share price of ZIL was ₹103.55. As stated in *interim order*, the share price of ZIL fell to ₹45 on November 30, 2011. Hence total loss, if any, suffered by shareholders (including promoters) would amount to ₹74.24 crore which is USD 11.69 million (arrived at by calculating the difference in share prices, ₹103.55 less ₹45, multiplied by total issued share capital of the company). Further, if the shareholding pattern of ZIL is taken into consideration, the notional loss, if any, suffered by the retail shareholders (holding approximately 14%) would be only ₹10.39 Crore (USD 1.67 million).

(v). The direction at para 25(ii) of the *interim order* is void *ab initio* as the same is tainted with legal impossibility as the noticees being the resident Indians, are prohibited under the Foreign Exchange Management Act, 1999 from obtaining any foreign currency guarantees as they can purchase foreign exchange up to only USD 200,000 under Liberalized Remittance Scheme.

(w). Mr. Vijay Ramchandra Mukhi, who was an independent director of ZIL at the relevant time, did not avail the opportunity of personal hearing but submitted his reply vide letter dated January 28, 2014 stating *inter alia* that he was only an independent and non-executive director of ZIL and was not privy to any discussion that transpired between the promoters/executive directors of ZIL and the FCCB holders. Further, he was not responsible for any of the acts as alleged in the *interim order*.

9. I have carefully considered the replies and submissions of the noticees. The noticees have contended that the copies of the complaints referred to in the *interim order* have not been provided to them and thus, the proceedings are vitiated on account of non observance of principles of natural justice. In this regard, I note that the said complaints are neither the basis nor they have been relied upon in the instant proceedings. The *interim order* has been passed on the basis of findings and observation of preliminary inquiry undertaken by SEBI on receipt of the complaints. I, therefore, find that no prejudice would be caused to the noticees by not furnishing the copies thereof.

10. I further note that the *interim order* clearly brings out the reasons for passing the preventive and remedial directions contained therein. It is pertinent to mention that the *interim order* has been passed in the course of preliminary inquiry and the investigation in the matter is ongoing. During the preliminary inquiry ZIL was given opportunity to submit explanations on the issues involved in the case and it had made submissions that have been duly dealt with in the *interim order*. Thus, ZIL and the noticees who are in charge of affairs of ZIL were well aware about SEBI's inquiry in the matter and cannot be said to be taken by surprise by the *interim order*. Further, the *interim order* has been issued in the nature of show cause notice affording the noticees a post decisional opportunity to file their replies and avail the opportunity of personal hearing. Such exercise of power is specifically permitted under section 11 and 11B of the SEBI

Act and the position that it is not necessary to give pre-decisional hearings in the cases of *ad-interim ex-parte orders*, has also been settled by various judgments such as the matter of *Anand Rathi & Others Vs. SEBI (2002 (2) Bom CR 403*, wherein the Hon'ble Bombay High Court has held as under:

> *" 31. It is thus clearly seen that pre decisional natural justice is not always necessary when ad-interim orders are made pending investigation or enquiry, unless so provided by the statute and rules of natural justice would be satisfied if the affected party is given post decisional hearing. It is not that natural justice is not attracted when the orders of suspension or like orders of interim nature are made. The distinction is that it is not always necessary to grant prior opportunity of hearing when ad-interim orders are made and principles of natural justice will be satisfied if post decisional hearing is given if demanded.*
>
> *32. Thus, it is a settled position that while ex parte interim orders may always be made without a pre decisional opportunity or without the order itself providing for a post decisional opportunity, the principles of natural justice which are never excluded will be satisfied if a post decisional opportunity is given, if demanded."*

11. Further, the Hon'ble High Court of Judicature for Rajasthan at Jaipur in the matter *M/s. Avon Realcon Pvt. Ltd. & Ors Vs. Union of India & Ors* (D.B. Civil WP No. 5135/2010 Raj HC) has held that:

> *"…Perusal of the provisions of Sections 11(4) & 11(B) shows that the Board is given powers to take few measures either pending investigation or enquiry or on its completion. The Second Proviso to Section 11, however, makes it clear that either before or after passing of the orders, intermediaries or persons concerned would be given opportunity of hearing. In the light of aforesaid, it cannot be said that there is absolute elimination of the principles of natural justice. Even if, the facts of this case are looked into, after passing the impugned order, petitioners were called upon to submit their objections within a period of 21 days. This is to provide opportunity of hearing to the petitioners before final decision is taken. Hence, in this case itself absolute elimination of principles of natural justice does not exist. The fact, however, remains as to whether post-decisional hearing can be a substitute for pre-decisional hearing. It is a settled law that unless a statutory provision either specifically or by necessary implication excludes the application of principles of natural justice, the requirement of giving reasonable opportunity exists before an order is made. The case herein is that by statutory provision, principles of natural justice are adhered to after orders are passed. This is to achieve the object of SEBI Act. Interim orders are passed by the Court, Tribunal and Quasi Judicial Authority in given facts and circumstances of the case showing urgency or emergent situation. This cannot be said to be elimination of the principles of natural justice or if ex-parte orders are passed, then to say that objections thereupon would amount to post-decisional hearing. Second Proviso to Section 11 of the SEBI Act provides adequate safeguards for adhering to the principles of natural justice, which otherwise is a case herein also…"*

12. In view of the above, I find that the principles of natural justice have been duly complied with in this matter. I further note that instead of availing the opportunity provided by the *interim order* the noticees chose to challenge the *interim order* before the Hon'ble SAT. Even after the order of the Hon'ble SAT dated July 23, 2013 was stayed by the Hon'ble Supreme Court on August 27, 2013 the noticees did not avail the opportunity to file reply till January 28, 2014 when the reply was sent by the noticees on receipt of notice of hearing sent by SEBI.

13. Mr. Vijay Ramchandra Mukhi has submitted that he was only an independent and non-executive director of ZIL and was not privy to any discussion that transpired between the promoters/executive directors of ZIL and the FCCB holders. Further, he was not responsible for any of the acts as alleged in the *interim order*. I have perused the 15th and 16th Annual Report for the year 2010- 2011 and 2011-12, respectively of ZIL as available on BSE website and submitted by the noticees. It is noted that Mr. Vijay Ramchandra Mukhi was part of board of directors of ZIL at the relevant time and had attended all the board meetings during the year 2010-11 including the board meeting held on December 27, 2010 wherein the board of directors of ZIL had decided to raise the funds for re-payment/redemption of FCCBs due in August 2011 and August 2012 and to call EGM for obtaining shareholders' approval for borrowing monies upto ₹ 1,500 Crores. Further, he was the chairperson of the Audit Committee of ZIL for the aforesaid period and has attended all the meetings of Audit Committee held during the year 2011-2012. It is quite strange to observe that the Audit Committee has not commented upon the manner in which the sale proceeds of MSD business were utilised.

14. In view of these facts and circumstances, I find that Mr. Vijay Ramchandra Mukhi was aware of the utilization of monies by the promoters/directors of ZIL and such utilisation of monies was done with his complicity and acquiescence. Thus, he cannot escape from the obligation of the board of directors with regard to their fiduciary duties towards ZIL and its shareholders. In this regard, the observation of the Hon'ble SAT in the matter of *Mr. N Narayanan vs SEBI* (order dated October 05, 2012) is worth mentioning:

> *"With the changing scenario in the corporate world the concept of corporate responsibilities is also rapidly changing day by day. The director of a company cannot confine himself to lending his name to the company but taking light responsibility for its day to day management. While functions may be delegated to professionals, the duty of care, diligence, verification of critical points by directors cannot be abdicated. The directors are expected to have a hands on approach in the running of the company and take up responsibility not only for the achievements of the company but also the failings thereto."*

15. In order to deal with other contentions of the noticees, I deem it necessary to briefly refer to the background under which the *interim order* has been passed. I note that the *prima facie* findings have been given in the *interim order*, *inter alia*, in view of the following facts and circumstances:

"(a) The two series of FCCBs issued by ZIL due for redemption in August 2011 and August 2012 had terms of cross default stipulating that default in redemption of FCCBs due in August 2011 would automatically cause a cross default on ZIL's obligation on the other series of FCCBs due for redemption in August 2012. ZIL and its promoters/directors, despite being fully aware of the terms of FCCBs and having approval of shareholders to redeem them, chose to divert the sale proceeds of MSD Division to their related entities

(b) The default with regard to redemption of FCCBs had occurred on September 21, 2011. ZIL and its promoters/ directors did not inform the BSE/NSE about failure to redeem the FCCBs and they tried to hide the information about default until intervention by exchanges on October 13, 2011.

(c) The claim of ZIL, as submitted in its letters dated October 13, 2011 to BSE/NSE and December 10, 2011 to SEBI, that it was in negotiations with the FCCB holders to extend the time for redemption of FCCBs. It has been brought to SEBI's notice that FCCB holders have filed a suit against ZIL for recovery on October 21, 2011 and have also filed a winding up petition against ZIL. Thus, such disclosure by ZIL was prima facie false and misleading.

(d) ZIL and its promoters/directors also failed to inform the exchanges and the shareholders about this material litigation against ZIL, thereby concealing this fact.

(e) The disclosure, made on October 13, 2011 to BSE that ZIL planned to utilize sale proceeds of MSD Division for partial repayment of FCCBs is also false and misleading as the proceeds have not been used for this purpose at all. This disclosure also suggests misrepresentation of material fact of default of redemption.

(f) The information about the amount of receipt of sale proceeds of MSD Division and the way in which it was utilized was concealed by ZIL and its promoters/directors. The fact that VU Dubai and Cloud Dubai were promoter related entities at the time of transfer of USD 13 million to them and were acquired to make them subsidiaries of ZIL was not disclosed to the stock exchanges, but came to notice of SEBI through complaints and media publications. ZIL and its promoters/directors did not seek the approval of shareholders for acquisition of these new companies, which was in contradiction to the original approval of the shareholders.

(g) ZIL and its promoters/directors diverted the sale proceeds of MSD Division for myriad purposes other than that of redemption of FCCBs, as approved by its shareholders.

(h) While examining the claim of ZIL regarding its financial soundness and ability to pay back FCCB holders, Hon'ble Bombay High Court, vide its order dated July 09, 2012 rejected the valuation of ZIL (cloud computing business) arrived at ₹598 crores and found the worth of ZIL to be in the range of ₹152- ₹211crores only."

16. It has been observed in the *interim order* that the sequence of events and pattern of transactions in this case *prima facie* indicate that ZIL and its promoters/directors not only wantonly defaulted in redemption of FCCBs and disregarded shareholders' resolution but also adopted fraudulent device and artifice to defraud the shareholders of ZIL. In the *interim order* it has been *prima facie* found that ZIL and its promoters/directors made promise to the shareholders without

intending to perform the same. It has also been alleged that they made *prima facie* false and misleading disclosures, misrepresented material fact and concealed the material information from the stock exchange and public, etc. and thus, they employed a device or artifice to fraudulently divert the sale proceeds of its MSD business and the aforesaid facts *prima facie* indicate that the acts, omissions and concealment of ZIL and its promoters/directors were *'fraudulent'* as defined in regulation 2(1)(c) of the PFUTP Regulations.

17. In the *interim order* it has been further *prima facie* found that the noticees stripped the assets of ZIL for the benefit/ interest of companies/entities controlled by them in fraudulent and deceitful manner which led to the following consequences:-

    a. Shareholders/investors lost considerable amount of money as a result of sharp price fall in the scrip of ZIL from approximately ₹190 on September 23, 2011 to approximately ₹45 on November 30, 2011 i.e. a fall of approximately 75% in just 45 trading days.
    b. The shareholders' value got eroded because of the misconduct of the promoters/directors.
    c. ZIL remained fastened with the liability to pay back the FCCB holders leading to further financial burden on the shareholders' wealth in ZIL.

18. Thus, it is very clear from the *interim order* that SEBI has not sought to enforce any of the provisions of the Companies Act, 1956 including those specified under section 55A thereof i.e. issue and transfer of securities and non-payment of dividend, rather, it deals with the *prima facie* fraudulent activities relating to the securities market which are prohibited under the SEBI Act and the PFUTP Regulations. The subject matter of the *interim order* is the protection of the interests of investors in securities including the shareholders of ZIL and integrity of the securities market which are exclusively the domain of SEBI under the SEBI Act as far as a listed company like ZIL is concerned. The *interim order* also does not seek to enforce the right of redemption of the FCCBs holders as contended. In fact, the *interim order* (in its para. 26) has very clearly provided that the directions contained therein are "*without prejudice to the rights of FCCB holders to enforce their rights of redemption against ZIL before competent authority, forum or court."* The direction in para 25(ii) of the *interim order* envisages that the bank guarantee may be invoked should any adverse inference is drawn by SEBI in its final order with regard to the actions of the promoters/board of directors of ZIL in diverting the sale proceeds of MSD business and SEBI deems it necessary to compensate ZIL. Thus, it is very clear that the *interim order* has not sought to compensate FCCB holders as contended by the noticees. For the same reasons, I find that the *interim order* has not sought to enforce the shareholders' resolution as contented by the noticees. However, non-implementation of shareholders resolution, if done as a part of fraudulent and manipulative device to defraud the investors and securities market as *prima facie* found in the *interim order*, would exclusively fall within the domain of SEBI in view of provisions

of section 11(2)(e) and 12A of the SEBI Act. I, therefore, reject the contentions of the noticees in this regard also.

19. The noticees have further contended that the matter covered under the *interim order* is *sub judice* and is the subject matter of Civil Suit No. 2865 of 2011 and Company Petition no. 28 of 2012 between the trustees for FCCB holders and ZIL before the Hon'ble Bombay High Court and that the Hon'ble Bombay High Court has given adequate protection to the FCCB holders and SEBI need not interfere in the matter. I note that the said civil suit pending before the Hon'ble Bombay High Court has arisen out of the contractual dispute between the creditors (FCCB holders) and ZIL. Similarly, the winding up petition has also been filed by the creditors against ZIL in respect of their unpaid claim. It is noted that in those proceedings before the Hon'ble Bombay High Court the fraud perpetrated on the investors in securities including the shareholders of ZIL and the market integrity is not the issue for determination by Hon'ble High Court and hence, the issues involved in the instant proceedings are not *sub judice* before any court. In my view there is no embargo imposed by any law or judgment of any court on the instant proceedings which are different and independent from those pending before the Hon'ble High Court. I, therefore, reject the contentions of the noticees in this regard.

20. Further, the SEBI FAQ relied upon by the noticees is relevant only to the private investor grievances/complaints involving the matters such as non-payment of dividend, non-receipt of share certificate, non-transfer of shares, etc. The FAQ does not apply to the proceedings initiated by SEBI with regard to investor protection in general and safeguarding the integrity of market as against the fraudulent and unfair trade practices undertaken by any other person. In the instant case, the matters dealt with in the *interim order* were not *sub judice* before any court at the time when the *interim order* was passed. With regard to the jurisdiction of MCA on the investor grievances pertaining to mis-management of company, minority shareholders' interests as stated in the FAQ, it needs to be mentioned here that the *interim order* does not intend to redress the minority shareholders grievances/complaints relating to the matters stated in the FAQ. It also does not proceed to enforcement of shareholders' resolution as contended by the noticees. It is very clear from the *interim order* that the issues dealt therein pertain to the alleged fraudulent acts, omissions and *mala fide* conduct of the noticees which were *prima facie* found to be in contravention of securities laws which are to be enforced exclusively by SEBI. The issues involved in the instant matter have wide ramifications for protection of interests of investors and securities market and for safeguarding the market integrity. In addition, the failure in discharge of fiduciary duties by the noticees also impacts the corporate governance in listed company for which SEBI is also concerned in addition to the MCA. I, therefore, find that the reliance of the noticees on the said FAQ is misplaced.

21. I further note that the submissions of SEBI in the appeal before the Hon'ble SAT were made in the context of the *prima facie* fraudulent activities of the noticees relating to the securities market.

The said statement was made in light of the fact that the *interim order* specifically dealt with the allegation of fraudulent activities of the noticees and it was passed in the interests of investors in securities and integrity of the securities market - the matters not dealt in the proceedings before the Hon'ble High Court. Also, in the injunction order dated October 09, 2012 no personal obligation /liability was imposed upon promoters/directors of ZIL for their fraudulent acts and dishonest conduct as alleged in the interim order. I, therefore do not agree with the noticees contention in this regard.

22. With regard to the contentions of the noticees as to scope and ambit of powers of SEBI under section 11(1), 11(4) and 11(B) of the SEBI Act, I note that the scheme of the Act is very clear. It is pertinent to mention the relevant provisions which are as under:

Functions of Board.

11. (1) Subject to the provisions of this Act, it shall be the duty of the Board to protect the interests of investors in securities and to promote the development of, and to regulate the securities market, by such measures as it thinks fit.

(2) Without prejudice to the generality of the foregoing provisions, the measures referred to therein may provide for—

.....

(e) prohibiting fraudulent and unfair trade practices relating to securities markets;

……..

(4) Without prejudice to the provisions contained in sub-sections (1), (2), (2A) and (3) and section 11B, the Board may, by an order, for reasons to be recorded in writing, in the interests of investors or securities market, take any of the following measures, either pending investigation or inquiry or on completion of such investigation or inquiry, namely:—

(a) suspend the trading of any security in a recognised stock exchange;

(b) restrain persons from accessing the securities market and prohibit any person associated with securities market to buy, sell or deal in securities;

(c) suspend any office-bearer of any stock exchange or self-regulatory organisation from holding such position;

(d) impound and retain the proceeds or securities in respect of any transaction which is under investigation;

(e) attach, after passing of an order on an application made for approval by the Judicial Magistrate of the first class having jurisdiction, for a period not exceeding one month, one or more bank account or accounts of any intermediary or any person associated with the securities market in any manner involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder:

Provided that only the bank account or accounts or any transaction entered therein, so far as it relates to the proceeds actually involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder shall be allowed to be attached;

(f) direct any intermediary or any person associated with the securities market in any manner not to dispose of or alienate an asset forming part of any transaction which is under investigation :

Provided that the Board may, without prejudice to the provisions contained in sub-section (2) or sub-section (2A), take any of the measures specified in clause (d) or clause (e) or clause (f), in respect of any listed public company or a public company (not being intermediaries referred to in section 12) which intends to get its securities listed on any recognised stock exchange where the Board has reasonable grounds to believe that such company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market :

Provided further that the Board shall, either before or after passing such orders, give an opportunity of hearing to such intermediaries or persons concerned.

Power to issue directions.

11B. Save as otherwise provided in section 11, if after making or causing to be made an enquiry, the Board is satisfied that it is necessary,—

(i) in the interest of investors, or orderly development of securities market; or

(ii) to prevent the affairs of any intermediary or other persons referred to in section 12 being conducted in a manner detrimental to the interest of investors or securities market; or

(iii) to secure the proper management of any such intermediary or person it may issue such directions,—

(a) to any person or class of persons referred to in section 12, or associated with the securities market; or

(b) to any company in respect of matters specified in section 11A, as may be appropriate in the interests of investors in securities and the securities market.

23. It is settled position that the above provisions are unambiguous with respect to scope and ambit of SEBI's jurisdiction, and power to issue *interim* as well as final directions under section 11 and 11B of the SEBI Act, pending inquiry or investigations. It is also settled position that both the sections are interconnected and co-extensive and the provisions of those sections are enabling provisions for the purpose of protection of interests of investors in the securities and the securities market. Further, the power conferred under those sections is of widest possible amplitude. In this regard, I deem it relevant to refer to few judgments of the Hon'ble SAT, the Hon'ble High Courts and the Hon'ble Supreme Court in the following paragraphs:-

(a). In *Bank of Baroda Limited* v. *SEBI(*2000) 26 SCL 532, the Hon'ble SAT held that:

"*Section 11 and 11B are interconnected and co-extensive as both these sections are mainly focused on investor protection. On a careful perusal of the said section 11 it could be seen that the SEBI has been in no uncertain terms mandated to protect the interest of the investors in securities by such measures as it thinks fit. However, the power under Section 11 is not unlimited. The Legislature has circumscribed this power, by putting the caveat that these measures are subject to the provisions of the Act. The ambit of power is contained within the framework of the Act. But within the statutory framework such power reigns.*"

(b). In the matter of *Ramrakh R. Bohra* v. *SEBI* [1999] 96 Comp Cas 623 (Bom) the Hon'ble Bombay High Court held as under :-

"Section 11B is an enabling provision enacted to empower SEBI to protect interest of investors and to promote the development of and to regulate the securities market and to prevent malpractices and manipulations inter alia by brokers. Such an enabling provision must be construed so as to subserve the purpose for which it is enacted. It would be the duty of the court to further the legislative object of providing a remedy for the mischief. A construction which advances this object should be preferred rather than one which attempts to find a way to circumvent it.

The said power to issue directions under Section 11B must carry with it, by necessary implication, all powers and duties incidental and necessary to make the exercise of these powers fully effective including the power to pass interim orders in aid of the final orders. ....."

In this case, the Hon'ble Bombay High Court further held that -

"28. If one has regard to the aforesaid principles, it would follow that the power which has been conferred by Section 11B to issue directions are of the widest possible amplitude and are exercisable in the interest of investors and in order to prevent, inter alia, a broker from conducting his business in a manner detrimental to the interests of the investors or the securities market. The said power to issue directions under Section 11B must carry with it, by necessary implication, all powers and duties incidental and necessary to make the exercise of these posers fully effective including the power to pass interim orders in aid of the final orders."

(c). In the matter of *Anand Rathi & Others Vs. SEBI (2002 (2) Bom CR 403)*, the Hon'ble Bombay High Court has upheld the powers of SEBI to pass such orders under sections 11 and 11B of the SEBI Act as under:-

"While considering the question as to whether the SEBI has authority of law under Sections 11 and 11B to order interim suspension, we have to bear in mind that SEBI is invested with statutory powers to regulate securities market with the object of ensuring investors protection, orderly and healthy growth of securities market so as to make SEBI's control, over the capital market to be effective and meaningful. It cannot be gainsaid that SEBI has to regulate speculative market and in case of speculative market varied situations may arise and looking into the exigencies and requirements, it has been entrusted with the duty and functions to take such measures as it thinks fit. Section 11B is an enabling provision enacted to empower the SEBI Board to regulate securities market in order to protect the interest of the investors. Such an enabling provision must be so construed as to subserve the purpose for which it has been enacted. It is well settled principle of statutory construction that it is the duty of the Court to further Parliament's aim of providing of a remedy for the mischief against which enactment is directed and the Court should prefer construction which will suppress the mischief and advance remedy and avoid evasions for the continuance of the mischief."

(d). In the matter of *Karvy Stock Broking Ltd. Vs. SEBI.* Appeal No.92 of 2006 the Hon'ble SAT held as under:

"The introduction of sub section (4) in section 11 and various other provisions like section 11B is indicative of the legislative intent. These provisions are meant to arm the Board with authority so as to be able to effectively exercise power and achieve the declared objectives of the Act.

..……

We cannot lose sight of the fact that the Board has to regulate a speculative market and in such a market varied situations may arise all of which cannot be envisaged and there may be an urgent need to pass an order even when an inquiry or investigation is pending. ……..

On an examination of the provisions as noticed above, we find that the legislative scheme is clear. The provisions of the Act are basically intended to protect the interests of the investors and to promote the market. However, the Act as initially enacted provided primarily for taking promotional or protective measures. The power to take preventive or punitive measures was implicit…….....……

Now it has been expressly extended to taking even the preventive or punitive measures. Without doubt, these, too, are ultimately aimed at achieving the basic objectives of investor protection and promotion of the development and regulation of the securities market as contained in the preamble.

……

In view of the above, we hold that the word 'inquiry' used in section 11(4) refers to the inquiries held under sections 11, 11B, also to the enquiry under the inquiry regulations framed under section 12(3) and also to the inquiry held under Chapter VIA and it is during the pendency of any of these inquiries that an interim order could be passed with a view to protect the interests of investors or in the interest of the market."

(e). The Hon'ble Supreme Court in the matter of *SEBI vs Ajay Agarwal* (Civil Appeal No.1697 of 2005) held as under:

" 41. It is a well known canon of construction that when Court is called upon to interpret provisions of a social welfare legislation the paramount duty of the Court is to adopt such an interpretation as to further the purposes of law and if possible eschew the one which frustrates it.

42. Keeping this principle in mind if we analyse some of the provisions of the Act it appears that the Board has been established under Section 3 as a body corporate and the powers and functions of the Board have been clearly stated in Chapter IV and under Section 11 of the said Act.

43. A perusal of Section 11, Sub-Section 2(a) of the said Act makes it clear that the primary function of the Board is to regulate the business in stock exchanges and any other securities markets and in order to do so it has been entrusted with various powers.

……. Sub Section (4) of Section 11 of the said Act, which gives the Board the power to restrain persons from accessing the securities market and to prohibit such persons from being associated with securities market to buy and sell or deal in securities."

24. It is trite to say that section 11(1) of the SEBI Act casts the duty on SEBI to protect the interests of the investors, promote development of and regulate the securities market, ***by such measures as it thinks fit***. Apart from this plenary power, section 11(2) of the SEBI Act enumerates illustrative list of measures that may be provided for by SEBI in order to achieve its objective. One of the measures enumerated in 11(2)(e) is *"prohibiting fraudulent and unfair trade practices relating to securities markets"*. The word *'measure*' has not been defined or explained under the SEBI Act. It is well settled position that this word has to be understood in the sense in which it is generally understood in the context of the powers conferred upon the concerned authority. According to *Corpus Juris Secundum, 'measure '* means- *'anything desired to be done with a view to the accomplishment of a purpose, a plan or course of action intended to obtain some object, any course of action proposed or adopted by the Government'*. Measure is also understood *'as a means to an end'*. From the provisions of section 11, it is clear that the purpose of section 11(2)(e) of the SEBI Act is to prohibit all fraudulent and unfair trade practices relating to the securities market and the Board may take any '*measures'* in order to achieve this purpose.

25. On careful reading of the above provisions of the SEBI Act, I note that the only circumference around SEBI's powers under section 11 and 11B is the SEBI Act itself. The *'measures'* and the directions under section 11 and 11B of the SEBI Act can be taken / issued for prohibiting the fraudulent and unfair trade practices relating to securities market and achieving the objective of investor protection, and promotion of and regulation of the securities market. Though section 11(4) lists certain specific measures that may be taken either pending investigation or inquiry or on completion of such investigation or inquiry, its provisions are without prejudice to the provisions of sub-sections (1), (2), (2A), (3) and section 11B. Thus, the provisions of section 11(4) are clarificatory and do not limit or restrict the scope of power under section 11 and 11B of the SEBI Act. From the scheme of the SEBI Act and above referred judgments it is very clear that the provisions of section 11 and 11B are not limited as sought to be contended by the noticees.

26. It is also a settled position that the directions under sections 11 and 11B can be issued to any person associated with the securities market, including a company which has its securities listed or proposes to list its securities on a recognised stock exchange and its board of directors. The powers under those sections are wide enough to cover any situation and is not limited to insider trading or fraudulent and unfair trade practices relating to dealing in securities. I further note that the proviso to section 11(4) of the SEBI Act is applicable only in case of direction to impound and retain the proceeds of securities and power of attachment of the bank account. Nonetheless, the proviso empowers the Board to take those actions against a listed company

and the company which intend to get listed on a recognized stock exchange, if such company indulges in insider trading or fraudulent or unfair trade practices relating to securities market. Thus, once it has been *prima facie* found that a listed company has been indulging in *'fraudulent and unfair trade practices relating to securities market'*, the Board has unfettered powers to invoke those sections in the interests of investors in securities and the securities market. It also needs to be mentioned here that the *interim order* is not exclusively under section 11(4) rather it derives its power from section 11 including sub-sections (1), (2) and (4) thereof and sections 11B, 12A of the SEBI Act and section 12A of the SCRA. I, therefore, do not agree with the contentions of the noticee with regard to the scope of powers under section 11 and 11B of the SEBI Act.

27. I further note that the provisions of section 12A of the SCRA is *pari materia* section 11B of the SEBI Act. Under the provisions of section 12A of the SCRA also SEBI may, *in the interest of investors, or orderly development of securities market* issue directions, *inter alia*, to a listed company. This power is not limited to stock exchange or clearing corporation as sought to be contended by the noticees. It is pertinent to mention that in the instant case, apart from the fraudulent activities as *prima facie* found in the *interim order,* the noticees have also been *prima facie* found to have contravened the provisions of clauses 21 and 36 of the listing agreement read with section 21 of the SCRA.I, therefore, find that the contention of the noticees regarding invoking power under section 12A of the SCRA is misplaced.

28. In this case, as discussed hereinabove, the purpose of the *interim order* is to achieve the objectives of investor protection and safeguarding the market integrity by enforcing the provisions of the SEBI Act and the SCRA. I, therefore, do not agree with the contentions of the noticees with regard to the scope of the *interim order* and the jurisdiction of SEBI in the matter.

29. There is no dispute as to the scope of the directions in para 25(i) of the *interim order*. However, with regard to the direction contained in para 25(ii) of the *interim order,* the noticees have contended that the direction to furnish the bank guarantee would amount to *interim* disgorgement or imposition of monetary penalty or attachment before judgment or mandatory injunction and cannot be possible as an *interim* measure. In this regard, I note that the *interim order* clearly brings out the necessity of this direction, i.e. to prevent further loss to shareholders' value due to stripping of asset and erosion of value of ZIL and also to preclude recurrence of such default and violations as *prima facie* found in the *interim order*. Once it has been *prima facie* found that the shareholders' value in ZIL had eroded on account of asset stripping and fraudulent diversion of funds to the entities owned and controlled by the noticees leaving the company liable to pay to the FCCB holders and the shareholders/investors have lost considerable amount of money as a result of sharp fall in the price of ZIL scrip as discussed in the *interim order*, it was incumbent to take preventive measures to protect the assets. I am of the view that this is not a case wherein only the restraint on buying, selling or dealing in securities would be sufficient to prevent the *prima facie* fraud relating to the securities market. It is settled

position that an order of disgorgement is passed to disgorge ill-gotten gains or loss averted. The bank guarantee as directed at para 25(ii) of the *interim order*, in my view, is not in the nature of disgorgement of ill-gotten gains or loss averted as contended by the noticees. The bank guarantee as directed in para 25(ii) of the *interim order* is only a means to ensure that the monies derived from the assets of the shareholders and *prima facie* fraudulently diverted to the controlled/connected entities of the noticees are protected/restored, in the event any adverse inference is drawn in the final order and SEBI deems it necessary to compensate ZIL. I note that the facts in the NSDL case are different from those of the present case. In the former, ill-gotten gain was involved whereas the instant case involves alleged fraudulent erosion of value of shareholders of ZIL and protection of assets of ZIL. I, therefore, do not agree with the contention that this direction is in the nature of *interim* disgorgement in aid of final order of disgorgement as contended by the noticees. For the same reasons, I do not agree with the contentions of the noticees that the directions in para 25(ii) of the *interim order* amount to imposition of monetary penalty or attachment before judgment or mandatory injunction as sought to be contended by the noticees.

30. I have perused the SEBI's orders dated December 28, 2011 relied upon by the noticees and note that those orders were passed by SEBI in the context of diversion of monies raised from public through IPOs by the concerned companies for objects other than those stated in the prospectus. In those cases, the direction to bring back the IPO proceeds have been given to ensure that the monies raised from public are utilized for the objects disclosed to them in the prospectus. In this case, the *ad interim* directions have been issued to the noticees on the basis of *prima facie* findings in the *interim order* that the noticees have acted *mala fide* and had fraudulently diverted the sale proceeds of MSD business to the related entities/ companies in which they had a substantial interest.

31. With regard to the contentions of the noticees on applicability of provisions of regulation 2(1)(c) and regulation 3 (c) and (d) of the PFUTP Regulations and section 12A of the SEBI Act, it is trite to say that the '*measure*' provided under section 11(2)(e) of the SEBI Act, i.e. *"prohibiting fraudulent and unfair trade practices relating to securities markets",* is not limited to buying and selling of securities, rather it includes all fraudulent and unfair trade practices relating to securities markets. The provisions of the PFUTP Regulations and section 12A of the SEBI Act are in addition to the provisions section 11(2)(e) and this plenary power cannot be given limited interpretation as sought to be given by the noticees otherwise, it will defeat whole objective of protection of interest of investors and promotion and regulation of securities market and would endanger market integrity.

32. I further find that the definition of '*fraud*' in regulation 2(1)(c) of the PFUTP Regulations is an inclusive one. It is inclusive with respect to act, expression, omission or concealment committed by any person whether in deceitful manner or not, while dealing in securities in order

to induce another person. The definition is also inclusive with respect to '*knowing misrepresentation*', '*concealment of material fact*', '*suggestion to an untrue fact*', '*active concealment of fact with knowledge*', '*promise without intention to perform*', '*reckless and careless representations*', '*deceptive behaviour*', '*false statement*', etc. as listed in points (1) to (8) of regulation 2(1) (c). The *'dealing in securities'* by a person to induce another person to deal in securities is not *sine qua non* for the fraudulent activities listed in regulation 2(1)(c) (1) to (8). It is pertinent to note that the noticees' acts, omissions and conduct as described in the *interim order* particularly paras 15, 16, 19 and 20 thereof include making promise without intention to perform, willful concealment of material facts, false and misleading disclosures, misrepresentation of material facts, etc. In my view, the acts, omissions and conduct of the noticees as *prima facie* found in this case are squarely covered in the definition under the definition of *'fraud'* under regulation 2(1) (c) and their fraudulent, alleged manipulative and deceptive devices have to be construed accordingly.

33. I note that the provisions of section 12A of the SEBI Act and regulation 3 (c) and (d) of the PFUTP Regulations prohibit employment of any *'device'*, *'scheme'* or *'artifice'* to defraud '*in connection with dealing in securities'*; and engaging in any act, practice, course of business which operates or would operate as fraud or deceit upon any person '*in connection with dealing in securities'*. The words *'device'*, *'scheme'* or *'artifice'* have not been defined in the SEBI Act or in the PFUTP Regulations. According to the Black's Law Dictionary-

    (i) *"device"* means-

        (a) an invention or contrivance; any result of design;

        (b) a scheme to trick or deceive; a stratagem or artifice, as in the law relating to fraud.

    (ii) *"scheme"* means -

        (a) a systemic plan; a connected or orderly arrangement, especially of related concepts;

        (b) an artful plot or plan, usually to deceive others; a scheme to defraud creditors

    (iii) *"artifice"* means a clever plan or idea, especially one intended to deceive.

34. The expression '*in connection with dealing in securities'* in section 12A (b) and (c) of the SEBI Act and regulation 3(c) and (d) of the PFUTP Regulations does not signify that the person employing the device, etc. and engaging in act, practice, etc. should actually buy or sell or deal securities. In my view, the words '*in connection with dealing in securities'* for this purpose will include any fraudulent, manipulative or deceptive device, e.g. false corporate announcements, false disclosures, promises without intending to perform, active concealment of a fact, knowing misrepresentation, reckless representations, etc. I, therefore, find that the acts, omissions and conduct of the noticees alleged in the *interim order* are covered within the scope of the expressions *"device"* or *"artifice"* or *"scheme" to defraud in connection with dealing in securities'*. In my view, any fraudulent or deceptive device, scheme, act, practice which has the potential to induce sale or purchase of or dealing in securities or to influence the investment decisions of the investors would be covered in the prohibitions of section 12A (b) and (c) of the SEBI Act and regulation

3(c) and (d) of the PFUTP Regulations. In this regard, it would be worthwhile to refer to the following observations made by the Hon'ble SAT in matter of V. *Natarajan vs. SEBI (Order dated June 29, 2011 in Appeal no. 104 of 2011)*:

> *"… we are satisfied that the provisions of Regulations 3 and 4 of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market), Regulations, 2003 were violated. These regulations, among others, prohibit any person from employing any device, scheme or artifice to defraud in connection with dealing in or issue of securities which are listed or proposed to be listed on an exchange. They also prohibit persons from engaging in any act, practice, and course of business which operates or would operate as fraud or deceit upon any person in connection with any dealing in or issue of securities that are listed on stock exchanges.*
>
> *These regulations also prohibit persons from indulging in a fraudulent or unfair trade practice in securities which includes publishing any information which is not true or which he does not believe to be true. Any advertisement that is misleading or contains information in a distorted manner which may influence the decision of the investors is also an unfair trade practice in securities which is prohibited. The regulations also make it clear that planting false or misleading news which may induce the public for selling or purchasing securities would also come within the ambit of unfair trade practice in securities...."*

35. In this case, it is alleged in the *interim order* that as news of probable default in redemption of FCCBs spread in the market, the share price of ZIL fell sharply from ₹190 on September 23, 2011 to approximately ₹45 on November 30, 2011 i.e. a fall of approximately 75% in just 45 trading days (as per BSE data). Even for the period from September 23, 2011 to October 13, 2011 (i.e. the day of disclosure of default on FCCBs by ZIL) the price of the scrip fell by half i.e. from ₹190 to ₹ 93. Moreover, there was a marked decline in the shareholding of Institutional Investors from 20.17% to 11.96% during the quarter ending September 2011 to December 2011. Thus, it can be safely inferred that the acts, omissions and conduct of the noticees as alleged in the *interim order* had potential to influence the price of the scrip and had induced buying /selling therein. I also hold that the *interim order* has not been passed in the context of dealing in FCCBs as has been contended by the noticees.

36. I, therefore, find that in order to charge the contravention of section 12A and regulation 3(c) and (d) of the PFUTP Regulations it is not necessary to allege that the person has indulged in manipulative devices while dealing in securities as contended by the noticees. If the interpretation forwarded by the noticees is accepted then the whole purpose of section 11(2)(e) of the SEBI Act and intent of the prohibitions under section 12A and regulations 3 (c) and (d) of the PFUTP Regulations shall be defeated. In this regard, the following observations of the Hon'ble SAT in the matter of Appeal no. 29 of 2012 in *Mr. N Narayanan vs SEBI* is worth mentioning:

"The appellants' learned counsel drew our attention to the provisions of the Act and FUTP Regulations and submitted that the appellants have not 'dealt in' the shares of the company, nor have they directly indulged in any device which would attract the provisions of the Act and the FUTP Regulations. We cannot accept the above contention. The provisions of section 12A of the Act and regulation 2(c) of the FUTP Regulations squarely cover the facts of the case. The appellants have employed a device so as to defraud investors in dealing in the securities. They have also perpetrated fraud as defined in regulation 2(c) of the FUTP Regulations. We cannot restrict the above provisions to the narrow confines of 'dealing in securities' as canvassed by the appellants' learned counsel. The provisions of section 12A of the Act and the definition of fraud in regulation 2(c) of the FUTP Regulations are very wide in their scope and the device employed by the appellants squarely fall within the mischief."

37. It is noted that the above order of the Hon'ble SAT has been upheld by the Hon'ble Supreme Court in the matter of *N. Narayanan vs. Adjudicating Officer, SEBI,* in Civil Appeal Nos. 4112-4113 of 2013, (order dated April 26, 2013). I, therefore, am of the view that the narrow interpretation sought to be given by the noticees would render the powers of SEBI otiose as it would restrict the scope of prohibitions provided in the SEBI Act and the PFUTP Regulations and render in failure in duty to regulate and promote the securities market and safeguarding market integrity. I, therefore, do not agree with contentions of the noticees in this regard.

38. Now coming to the submissions of the noticees on merits of the case, the limited issue to be considered in this order is as to whether, based on the available material on record and after considering the submissions made by the noticees, the directions issued vide *ad - interim ex-parte* order need to be continued, revoked or modified in any manner. It is admitted fact that ZIL had raised USD 33 and USD 50 million by issuing FCCBs which were due for redemption in September 2011 and August 2012, respectively. It is also admitted position that the FCCBs had terms of cross-default stipulating that default in redemption of FCCBs due in August 2011 would automatically cause a cross default on ZIL's obligation on the other series of FCCBs due for redemption in August 2012. On January 06, 2011, ZIL published its notice of EGM dated December 27, 2010, alongwith the Explanatory Statement under section 173(2) of the Companies Act, 1956, on the websites of BSE/NSE calling for an EGM to be held on January 29, 2011.

39. However, the noticees have denied the allegation that the announcement dated December 27, 2010 was made as a promise without intending to perform. Further, they have contended that the said announcement was not misleading as the resolutions proposed in the notice of the EGM to be held on January 29, 2011 were general and inclusive and in those resolutions it was nowhere disclosed that they were for authorising raising of funds upto ₹1500 crore for redemption of FCCBs as alleged in the *interim order*. In this regard, I note from the notice dated December 27, 2010 that ZIL had proposed resolutions to its shareholders for following matters, namely-

(a) to authorise the board of directors of the company to borrow monies from the domestic market or through External Commercial Borrowings (ECBs) which together with the monies already borrowed by the company may exceed to the aggregate of its paid up capital and free reserves subject to maximum of ₹1500 crore;

(b) to authorise the board of directors of the company to sell and/or lease the business, divisions, subsidiaries (wholly or partly) of ZIL or any part of the immovable or movable properties of the company, upto an amount not exceeding ₹1000 crore; and

(c) to authorise the board of directors to finalise and execute the agreements, documents, deeds, etc. for giving effect to the resolution mentioned at point (b) above.

40. It is further noted that the explanatory statement pursuant to section 173(2) of the Companies Act, 1956 attached with the said notice categorically made following disclosures to the shareholders of ZIL and public (by way of corporate announcements on BSE and NSE):-

"The Company has issued Foreign Currency Convertible Bonds of USD 33 million in August, 20006 and ISD 50 million in August 2007. These Bonds would become due for repayment/redemption in August, 2011and August, 2012. The Board of Directors propose to augment the funds for the purpose in one or more of the following methods (including) through any combination thereof :

(i) To borrow moneys from Domestic markets and/or through External Commercial Borrowings up to an amount not exceeding ₹ 1,500,00,00,000/- (Rupees One Thousand Five Hundred Crores).
(ii) To sell and/or lease the business and/or divisions including the subsidiaries (wholly and partly) of the company and for that purpose to issue debt securities/bonds, etc, in the domestic or international markets, as permitted by law so as to redeem / re-pay the outstanding Foreign Currency Convertible Bonds which would come for re-payment / redemption in August, 2011 and August 2012.
....."

41. From the above disclosures in the statutory explanatory statement to the shareholders and announcements made to public on BSE and NSE it is abundantly clear that ZIL had proposed the aforesaid resolutions to its shareholders with promise to raise the funds for the purpose of repayment/redemption of 2011 FCCBs and 2012 FCCBs. It is on this premise the shareholders passed the resolutions on January 29, 2011. Thus, it is apparent that on January 29, 2011, shareholders of ZIL in its EGM approved the sale/lease of the business/divisions including the subsidiaries (wholly or partly) of ZIL for the purpose of utilization of the proceeds of sale/lease towards redemption of both the FCCBs issued by ZIL. It is pertinent to mention here that the above disclosures made to public through announcements to BSE and NSE were having price sensitive information for taking investment decisions by the investors.

42. It is undisputed fact that ZIL sold one of its MSD business to Zenith RMM LLC and out of the sale proceeds(USD 48 million) of MSD business, an amount of USD 33.93 million was diverted as under:–

    i. USD 13 million transferred to VU Dubai & Cloud Dubai;
    ii. USD 7.2 million and US$ 3.2 million transferred to Zenith Singapore;
    iii. USD 1.53 towards purchase of capital goods by Zenith Dubai;
    iv. USD 6 million to business creditors of ZIL;
    v. USD 3 million for purchase of capital goods by ZIL.

43. The noticees have contended that the above funds were so diverted because the funds could not be utilized for redemption of FCCBs as the trustees of FCCBs insisted payment under both the 2011 and 2012 FCCBs immediately in full. In this regard, I note that the 2011FCCBs were due for redemption on September 21, 2011. The sale proceeds of MSD business was received by ZIL and Zenith Dubai on September 27, 2011 and on the same date ZIL had received the first notice of default from the trustees and this notice was for redemption of 2011 FCCBs only. Thus, there was no insistence by trustees for redemption of both FCCBs in full as on September 27, 2011. Being aware of the obligation of ZIL to redeem 2011 FCCBs on September 21, 2011 and the term of cross-default, it was incumbent upon ZIL and its promoters/directors to immediately redeem the 2011 FCCBs from the sale proceeds of MSD business, as promised to shareholders and disclosed to public, at least on receipt of the notice of default on September 27, 2011. Therefore, the noticees should have honored their promise made to the shareholders of ZIL through their decision and announcement dated December 27, 2010 or at least should not have utilized the sale proceeds of MSD business for the purposes other than those promised to the shareholders and disclosed to public. In these circumstances, any person of ordinary prudence would have been more vigilant towards such redemption obligations rather than diverting the sale proceeds to related entities as *prima facie* found in the *interim order*. However, the noticees chose to divert the sale proceeds of MSD business for the purposes other than those promised to the shareholders and started doing so from September 29, 2011 onwards. I further note that it is only on September 30, 2011 that the trustees sent the notice for cross-default when the noticees had failed to fulfill their obligation towards FCCB holders despite having the sale proceeds of MSD business in their bank account as on that date. I note that the noticees had sufficient opportunity to redeem the 2011 FCCBs till at least September 30, 2011 when the sale proceeds of MSD business was available with them and till the notice for cross-default was issued by the trustees. In fact, the noticees had not shown any willingness to redeem 2011 FCCBs even after the receipt of notice of default. It is curious to note that despite having outstanding promise for performance and obligation to fulfill their fiduciary duties to the shareholders the noticees diverted substantial amount of the sale proceeds on September 29, 2011, September 30, 2011, October 03, 2011, October 05, 2011, October 06, 2011 and October 11, 2011, etc. It is noted that it is only on October 10, 2011, the trustees sent the demand notice citing cross-default stipulation. However, the noticees did not bother to honour even this notice

and continued to divert the sale proceeds. In fact, substantial chunk of the sale proceeds were diverted by the noticees before the demand notice for cross-default was sent by the trustees. I further note that the procedural requirement of obtaining RBI permission for premature redemption of 2012 FCCBs was to be fulfilled by ZIL. Such requirement does not impose any impossibility as sought to be contended by the noticees. In the facts and circumstances of this case, I do not see any compelling reasons to use the monies realized from sale of MSD business for any purpose – not the least for paying to group entities for various purposes – other than for redemption of FCCBs, which was the sole purpose for which approval of shareholders was taken and disclosures were made to public. The noticees have also not shown any material to show any genuine deliberation/negotiations with the FCCB holders as claimed. In view of these facts and circumstances, I do not find merit in these submissions of the noticees and hence, I reject all contentions and claims of the noticees in this regard.

44. The noticees have claimed in their reply dated January 28, 2014 that the alleged payments were made out of sale proceeds of MSD business after October 10, 2011 i.e. after the invocation of cross-default clause by the trustees and failure of negotiation amongst the trustees, the FCCB holders and the noticees. However, from the reply dated January 28, 2014 and documents submitted by them in support of their claim, it is noted that the noticees started disbursing the money from September 29, 2011 onwards for purposes other than those authorized by shareholders of ZIL, when they were obligated to utilize the same for redemption of 2011 FCCBs. I, therefore, find the claim of the noticees false and misleading. It is apparent that instead of honoring the promises made to the shareholders of ZIL the noticees started diverting the sale proceeds for purposes other than those promised to the shareholders even before the notice of cross default was issued by the trustees on September 30, 2011.

45. It is undisputed fact that out of the cash proceeds of USD 48 million, ZIL had received USD 21 million and Zenith Dubai, a wholly owned subsidiary of ZIL had received USD 27 million. From the replies dated January 28, 2014 and March 11, 2014, the noticees have admitted that out of total consideration MSD business, USD 48 million has been utilized as under:

Sl. No.	Particulars	Amount (in USD million)
1.	Transfer to Zenith Singapore (a wholly owned subsidiary of ZIL) for payment to be made to Standard Chartered Bank in respect of a secured working capital loan obtained by Zenith Singapore obtained from Standard Chartered Bank	10.40
2.	Payment of advance tax (estimated capital gains tax on sale of MSD business)	5.80
3.	Payments made to business creditors of ZIL	6.00
4.	Purchase of capital goods for ZIL	3.00
5.	Purchase of capital goods for Zenith Dubai	1.53
6.	Investment in Cloud Dubai in which Zenith Dubai (wholly owned subsidiary of ZIL prior to the sale of MSD business) holds 99.2% shareholding	5.80

7.	Investment in VU Dubai in which Zenith Dubai holds 93.58% shareholding	8.00
8.	Further payment to Standard Chartered Bank to completely repay working capital loan	2.20
9.	Unutilized monies lying with ZIL	6.07
Total		48.00

46. I note that the basis of allegation is not the unutilized monies (USD 6.07 million lying with ZIL) or payments of advance taxes amounting to USD 5.80 million or subsequent diversion of USD 2.2 million to Standard Chartered Bank as claimed by the noticees. In this order, I proceed to deal with alleged diversion of USD 33.93 million while other payments/diversions need to be looked into by the ongoing investigations. From the submissions and documents submitted by the noticees it is noted that Zenith Dubai had made purported payment/ investments worth USD 13 million in VU Dubai (USD 8 million) and Cloud Dubai (USD 5 million) which in turn had issued fresh equity shares to Zenith Dubai on account of these investments. Pursuant to these investments, shareholding of Zenith Dubai in VU Dubai and Cloud Dubai became 93.58% and 99.2%, respectively. Further, total USD 10.53 million were transferred to business creditors and towards purchase of capital goods by ZIL and Zenith Dubai. Admittedly, total USD 10.40 million was transferred to Zenith Singapore, a wholly owned subsidiary of ZIL, as following:-

(a). USD 3.2 million from ZIL; and
(b). USD 7.2 million by Zenith Dubai in two tranches of USD 4.3 million and USD 2.9 million.

47. It is undisputed fact that the noticees no. 1 to 6 hold 64.89% shareholding in ZIL. Zenith Dubai is 100% subsidiary of ZIL. At the time when funds were transferred by Zenith Dubai to VU Dubai on October 11, 2011 and October 12, 2011, Mr. Akash Rajkumar Saraf (Promoter and Managing Director of ZIL), Mr. Rajkumar Saraf (Promoter and Chairman-cum-director of ZIL) and Ms. Devita Rajkumar Saraf (Promoter) were together holding 100% shareholding and control in VU Dubai. Similarly, when the funds were transferred to Cloud Dubai on the same dates, Mr. Akash Rajkumar Saraf and Mr. Rajkumar Saraf were together holding 100% shareholding and control in Cloud Dubai. It is noted that Mr. Akash Rajkumar Saraf and Mr. Rajkumar Saraf were the promoters of the transferor (Zenith Dubai) as well as the transferee companies (VU Dubai and Cloud Dubai). Further, Ms. Devita Saraf daughter of Mr. Rajkumar Saraf is a promoter of ZIL as well as a promoter of VU Dubai. Therefore, it is apparent that the funds amounting to USD 13 million were transferred to the entities owned and controlled by the promoters of ZIL when the noticees, were under obligation to honour the promises made to the shareholders of ZIL. It is pertinent to note that the noticees were making investments out of sale proceeds of MSD business of ZIL in the promoter related companies situated out of India when ZIL having liability to fulfill the promises made to its shareholders with regard to redemption of FCCBs was called upon by the trustees to redeem the FCCBs.

48. In their reply dated January 28, 2014 the noticees have claimed that Zenith Dubai was allotted shares by VU Dubai and Cloud Dubai against the investment of USD8 million and USD 5 million in VU Dubai and Cloud Dubai, respectively. It is noted that the documents submitted by the noticees in respect of the issuance of new shares pursuant to the purported investments in VU Dubai and Cloud Dubai, do not clearly spell the reasons/purpose for such investments or substantiate the valuation of such investments or the networth of these transferee companies. In the said reply, the noticee have also claimed that Cloud Dubai has been closed and the entire money of USD 5 million has been repaid to Zenith Dubai, which in turn was paid to ZIL in April 2013 pursuant to the order of Hon'ble Bombay High Court. However, the noticees have not substantiated this claim by way of any evidence. It also remains unexplained as to how the money could be refunded on the closure of a company to the shareholder. I, therefore, am unable to accept these submissions and claims of the noticees. In the facts and circumstances of this case, such transfer of sale proceeds of MSD business of ZIL in companies related to the noticees in clandestine manner raises serious doubts about intention and conduct of the noticees.

49. Admittedly, the amount of USD 10.53 million was transferred for payment towards purchase of capital goods and secure creditors and not towards the purposes disclosed by ZIL. In my view, such expenses apparently are ongoing expenses incurred in the normal course of business by any company and cannot be said to be within scope of promises made by ZIL to its shareholders and disclosures made to public. Nonetheless, the documents submitted by the noticees suffer from deficiencies e.g. no invoices or the nature of services has been mentioned in respect of which the purported payments have been made by ZIL. I note that the admissions of the noticees reinforce the *prima facie* allegation that the sale proceeds were utilized for purposes other than those promised to the shareholders of in the explanatory statement to the notice of EGM and disclosed to public by corporate announcement made on BSE/NSE.

50. Admittedly, the amounts of USD 3.2 million and USD 7.2 million (in two tranches - USD 4.3 million and USD 2.9 million) were transferred from ZIL and Zenith Dubai, respectively to Zenith Singapore, a wholly owned subsidiary of ZIL. From the copy of the statement of account of ZIL submitted by the noticees, I note that the amount of USD 2.9 million was transferred from account of ZIL with State Bank of India, London branch to Zenith Singapore and not from the account of Zenith Dubai as has been contended by the noticees. The noticees have further admitted that they have transferred additional amount of USD 5.45 million out of the sale proceeds of MSD business to Zenith Singapore. The contention of the noticees is that such transfer of MSD business was for the purpose of repayment of working capital loan availed by Zenith Singapore from Standard Chartered bank, Singapore. Here again, it is pertinent to mention that such transfer of funds out of sale proceeds of MSD business was made in the subsidiary when ZIL, having liability to fulfill the promises made to its shareholders

with regard to redemption of FCCBs, was called upon by the trustees to redeem the FCCBs. In my view such diversion of sale proceeds of MSD business, in the facts and circumstances of this case, was not for the purpose promised to the shareholders and announced to public.

51. Another contention of the noticees is that the all the disclosures about the utilization of sale proceeds of MSD business was made in Annual Report of ZIL for the year 2011-2012. I note from the said Annual Report dated February 14, 2013 that the statements about non-redemption of FCCBs and litigations in that regard have been made therein. Further, VU Dubai and Cloud Dubai had been shown as subsidiaries of Zenith Dubai in the said Annual Report. However, in the said Annual Report, there is no mention of the manner in which sale proceeds of MSD business has been utilised by the noticees. Further, the disclosures made in the annual report in the year 2013 cannot be a substitute for the price sensitive disclosures that are required to be made promptly to the stock exchange/s under the listing agreement and the PIT Regulations. I, therefore, do not agree with the contentions of noticees in this regard.

52. In this case, admittedly, ZIL has failed to disclose the default in redemption of FCCBs to BSE/NSE within the time stipulated under the listing agreement and the PIT Regulations. According to the noticees clause 21 of the listing agreement does not have application in respect of FCCBs which are foreign bonds. I note that clause 21 of the listing agreement stipulates that the listed companies shall fix and notify the exchange at least 21 days in advance of the redemption date and amount payable on redemption of debentures and bonds and simultaneously issue cheques so as to reach the holders before the date of redemption. From the language of clause 21, it is clear that the said clause does not distinguish between domestic bonds and or foreign bonds as regards the obligation of the listed companies to make the requisite disclosures to the stock exchange and to send the cheque of redemption amount. It is pertinent to mention that the FCCB holders have option to acquire equity shares in the concerned listed company on conversion of FCCBs held by them. In fact , in the instant case, ZIL had earlier allotted equity shares to the FCCB holders on conversion of their bonds as disclosed in its annual report for the 2011-2012. The non-disclosures/wrong disclosures/distorted disclosures with regard to default on FCCB redemption, utilization of sale proceeds of MSD business and material litigation, etc., in this case, would surely lead to information asymmetry and defeat the purpose of disclosures stipulated under the listing agreement and PIT Regulations. I, therefore, do not agree with contentions of the noticees in this regard.

53. It is pertinent to mention that clause 36 of the listing agreement requires disclosure of information to the shareholders and public that have a bearing on the performance/operation of the company and that are price sensitive information. The information listed in clause 36 are inclusive. It is undisputed fact that the default in redemption of FCCBs, manner of utilisation of the sale proceeds of MSD business and material litigation i.e. suit and the winding up petition

filed by the FCCB holders were price sensitive information required to be disclosed under clause 36. The noticees have contended that they have made requisite disclosures on September 26, 2011 and October 13, 2011to BSE. In this regard, I note that the default in redemption of 2011 FCCBs had occurred on September 21, 2011. On September 26, 2011 ZIL had informed BSE regarding the sale of its MSD business but no disclosure about the default in redemption of FCCBs was made till the intervention of BSE on October 13, 2011. Even the disclosure made on October 13, 2011 was false as the default about redemption of 2012 FCCB on account of cross default stipulation was concealed from the said disclosure. Further, the disclosure on October 13, 2011 about the purported plan to utilise the sale proceeds for partial redemption of FCCBs was also false and misleading as substantial portion of sale proceeds was already diverted by October 11, 2011 and such diversion continued even thereafter. I, therefore, find that the announcement dated September 26, 2011 and the disclosures dated October 13, 2011 were not in compliance of clause 36 of the listing agreement and, in this case, the disclosures about default in redemption of FCCBs, manner of utilisation of the sale proceeds of MSD business and material litigation have not been disclosed to the stock exchanges in terms of clause 36. For the same reasons, I do not agree with the contentions of the notices that they had complied with the Code of Corporate Disclosure Practices for Prevention of Insider Trading provided in Schedule II the PIT Regulations. In the disclosure based regime, the disclosures of material information not only enable the investors to take informed investment decisions in the securities of the company but also provide the necessary tool for the regulators to ensure effective regulation, supervision and enforcement. The facts and circumstances of the case, *prima facie*, suggest that the concealment of facts and false, distorted and incomprehensible disclosure in this case were a ploy by the noticees to defraud the non-promoter shareholders of ZIL and investors in its scrip.

54. The noticees have further contended that the shareholders of ZIL in AGM held on March 28, 2013 ratified the above utilization of sale proceeds of MSD business as alleged in the *interim order*. The noticees have, however, not submitted any document in support of their claim. In this connection, I have perused the minutes of AGM of ZIL held on March 28, 2013 (as available on BSE website) which has happened after the passing of the *interim order* and note therefrom that with regard to the *interim order* a statement of Chairman of ZIL is recorded in the said minutes as under:-

> *" The Chairman, in his address, made special mention of the newspaper report of 26th March, 2013 in ' The Economic Times' of the ex-parte Interim Order dated 25th March , 2013 of the Securities and Exchange Board of India (SEBI) in respect of the Company's Issue of FCCBs of US $ 83 million and restraining the promoter from, inter alia buying, selling or dealing in the securities market till further directions. The company and the promoter group have not received the purported Order till date....."*

55. It is also noted that the Chairman of ZIL has mentioned in the said AGM about the suit filed by the FCCB holders in September 2011 and that the matter referred to in the news report in 'The Economic Times' against the promoters are *sub judice* in the Hon'ble Bombay High Court. He had also mentioned that SEBI order is beyond the jurisdiction of SEBI as the matter is already pending before the Hon'ble High Court. He had also asserted that ZIL, its promoters including promoter companies did not violate SEBI Act, its rules and regulations and the promoters had not dealt in company's shares since the last three years. He had also mentioned that ZIL is challenging SEBI order. In response to some members' queries, the Chairman of ZIL had commented with regard to audited accounts for the year ended 30th September, 2012 as following:

> *" We thank the Company and the staff for mailing the annual report in good time; the Company should challenge SEBI order and get the Company's name and its promoters' names cleared;..... we wish the Company comes out of the FCCB matters ..... "*

56. After the above discussions as noted in the minutes, following ordinary resolution was passed :

> *" RESOLVED THAT the Profit and Loss account for the year ended 30th September, 2012 and the Balance Sheet as at that date and the Reports of the Directors and the Auditors thereon be and are hereby received and adopted."*

57. I note from the minutes of the said AGM held on March 28, 2011 that there is neither discussion nor a resolution by shareholders to ratify the transfer of sale proceeds of MSD business for purposes other than those promised to the shareholders in the EGM dated January 29, 2011. In my view, therefore, the submissions of the noticees that by a resolution passed in the AGM held on March 28, 2013 the shareholders of ZIL had ratified the manner in which the sale proceeds of MSD business had been disbursed for the financial period ending September 30, 2012, are misleading.

58. The noticees have further contended that there is no allegation in the *interim order* that the board of directors of ZIL had acted *mala fide* or against the interest of ZIL. I note that the *interim order* particularly in para 15 and 20 specifically alleges *mala fide* on the part of the noticees on the basis of *prima facie* findings recorded therein. I, therefore, reject this contention of the noticees. I note that the thrust of the contention of noticees in their submissions is that the sale proceeds of MSD business were utilized for the interest of ZIL and it was not a *mala fide* use. I, however, note that the facts and circumstances mentioned in the *interim order* and discussed hereinabove, make it clear that the noticees have been dishonest and have acted *mala fide* in this case. The facts and circumstances leading to the inference of such conduct /intent / acts/omission of the noticees are summarised hereunder:

(i) The notice of EGM dated December 27, 2010 read with its statutory explanatory statement was very specific that the sale proceeds of MSD business shall be utilized for redemption of FCCBs only. The statement to that effect was made in the explanatory statement to the shareholders of ZIL and announced to the public at large by publishing the same on BSE/NSE. This was clearly a promise made to the investors including shareholders of ZIL.

(ii) The 2011 FCCBs were due for redemption by September 21, 2011. As per clause 21 of the listing agreement the advance notice of redemption date was to be given to the BSE/NSE and cheques for redemption amount were also to be sent to the bondholders 21 days before the due date of redemption. However, the cheques for redemption amount were not sent as stipulated in the listing agreement and terms of offer consequently, the default with regard to the 2011 FCCBs had occurred on September 21, 2011. This default also triggered the obligation for redemption of 2012 FCCBs in view of the cross-default stipulation. However, the noticees actively concealed the information about such default.

(iii) The sale proceeds of MSD business was received by ZIL and Zenith Dubai on September 27, 2011 and on the same day the trustees had sent the notice of default dated September 27, 2011 with regard to redemption of 2011 FCCBs. The noticees were aware of these obligations and for this purpose only the promises in the notice/explanatory statement dated December 27, 2010 were made. However, instead of fulfilling the promise, from September 29, 2011 onwards the noticees started diverting the sale proceeds for the purposes other than those promised and by October 11, 2011 substantial portion of sale proceeds were so diverted. From these facts it can be reasonably inferred that the noticees never intended to perform the promise made to the investors including the shareholders of ZIL.

(iv) The noticees also actively concealed the information about defaults in redemption of FCCBs until intervention by the exchanges on October 13, 2011 when disclosure of default of redemption of 2011 FCCB was made but the default of redemption of 2012 FCCBs was actively concealed. Even though the noticees had started diverting the sale proceeds from September 29, 2011 and substantial amount of sale proceeds were already diverted by October 11, 2011 it was disclosed to BSE on October 13, 2011 that ZIL plans to utilize sale proceeds of MSD business for partial repayment of FCCBs. Thus, such disclosure was false and misleading and suggested misrepresentation of material fact of default of redemption as the sale proceeds of MSD business were not used for the promised purpose at all.

(v) The trustees had sent the notice of cross default on September 30, 2011 when the noticees had failed to fulfil their obligations and promise despite having the sale proceeds in their bank account as on that date. On October 10, 2011 the trustees had sent the demand notice citing the cross default stipulation. However, they even did not

bother to honour any of the notices and diverted substantial amount of sale proceeds before the demand notice citing cross default was sent by the trustees. In fact the suit was filed by the trustee before the Hon'ble Bombay High Court on October 21, 2011. These facts and circumstances clearly suggest that there was no plausible negotiation between the trustee and the noticees. Therefore, the disclosure/representation to BSE, NSE and SEBI that ZIL in negotiation with FCCB holders to extend the time for redemption of FCCBs was false and misleading.

(vi) On one hand the above false and misleading disclosures/representations were being made and on the other hand the noticees continued to divert the sale proceeds. Hence, these disclosures/representations by the noticees were distorted disclosures and without any intent to act upon them. Further, the active concealment of material information by the noticees was used by them as an aid to execute the fraudulent device or artifice of the noticees.

(vii) The material fact about filing of suit and winding up petition by the trustees, being material litigations was not disclosed to the stock exchange and the shareholders. The diversion of sale proceeds of MSD business was also not disclosed to the stock exchanges and shareholders. Thus, the noticees have actively concealed the material fact.

(viii) In the AGM held on March 28, 2013, the shareholders of ZIL had not ratified the manner in which the sale proceeds of MSD business were utilized. However, the noticees have tried to mislead in these proceedings by making such submissions/representations.

(ix) There has been no disclosure on the exchanges with respect to investments made in VU Dubai and Cloud Dubai when the company was mandated to make such disclosures under the PIT Regulations and the listing agreement. Further, it is pertinent to note that VU Dubai and Cloud Dubai were promoter related entities at the time of investment and ZIL did not seek the approval of shareholders for acquisition of these new companies.

59. The above facts and circumstances indicate that the noticees have actively suppressed and concealed the actual facts and have represented false and distorted facts and indulged in '*suppressio veri* and *suggestio falsi*' which is a facet of *'fraud'* as defined in regulation 2(1) (c) of the PFUTP Regulations. Thus, the acts, omissions and conduct of the noticees as *prima facie* found in this case attract the prohibitions under section 12A (b) and (c) of the SEBI Act and regulations 3(c) and (d) of the PFUTP Regulations.

60. I am also of the view that the observations made by the Hon'ble Bombay High Court on the conduct of promoters/directors cannot be lost sight of while examining their conduct in their dealings which has a direct bearing on the integrity of the securities market and interests of investors including the shareholders of ZIL. In this regard, it is pertinent to mention here that

the Hon'ble Bombay High Court vide its order dated July 30, 2013 in the aforementioned company petition has observed as under:

> "*If at all the networth of the Company has been eroded, there is no doubt that the same is the creation of the Promoters/Directors of the Company who have siphoned away the moneys from the Company with the sole intention of avoiding repayment of the amounts due under the FCCBs.*"
>
> .....
>
> *"In view of thereof, though I have expressed my view, viz. that the promoters of the Company are absolutely dishonest and have siphoned away the funds of the Company in the manner set out in detail hereinabove and are responsible for the state of affairs of the Company prevalent as of date....."*

61. I further note that the appeal against the aforesaid order of the Hon'ble Single Judge was dismissed by a division bench of the Hon'ble Bombay High Court vide order dated September 02, 2013. It is also worth mentioning that while allowing the aforesaid company petition filed for winding up of ZIL, the Hon'ble Bombay High Court vide its order dated December 13, 2013 once again confirmed all the findings arrived at by the Hon'ble High Court in its abovementioned order dated July 30, 2013. In the said order dated December 30, 2013, the Hon'ble Bombay High Court has further observed that the promoters/directors of ZIL have not only been dishonest with the FCCB holders but have also been dishonest with the Hon'ble Court as they made a false and dishonest statement in court on oath *inter alia* stating that the sale proceeds received will be applied towards buyback/redemption of FCCBs but they had dishonestly utilized the said amounts. The findings of the Hon'ble Bombay High Court *qua* the noticees is as under:

> *"In fact, as set out hereinabove, the Promoters/Directors of the Company have not only been dishonest with the Bondholders and the Stock Exchange but have also been dishonest with the Court, and as stated hereinabove made a false and dishonest statement on oath in its affidavit dated 17th October, 2011, filed before the City Civil Court inter alia stating that the sale proceeds received will be applied towards buyback/redemption of FCCBs and have thereafter not paid a single paisa to the Bondholders and have dishonestly utilized the said amounts as set out hereinabove."*

62. According to the noticees, the fall in the prices of shares of ZIL cannot be attributed to their actions or inactions. As discussed hereinabove, the information about default in redemption of FCCBs, utilization of sale proceeds of MSD business and material litigation, etc. in this case was price sensitive information and had bearing on the affairs of ZIL and its share price. I do not find the contention of the noticees acceptable and do not find any reason to change the *prima facie* findings that the shareholders/investors had lost considerable amount of money as a result of sharp fall in the price of scrip of ZIL that had occurred due to spreading of news of probable default in redemption of FCCBs and thereafter actual default in redemption of FCCBs by ZIL. The noticees have not submitted any plausible and cogent defence against the *prima facie* findings regarding erosion in shareholders' value on account of misconduct of promoters/directors of

ZIL and that it remained fastened with liability to pay back the FCCB holders which will have financial burden on the shareholders. I do not find merit in the contention of the noticees that there is no stripping of assets of ZIL by the noticees since ZIL and its wholly owned subsidiaries were the beneficiaries of the sale proceeds of MSD business of ZIL because the sale proceeds have been fraudulently transferred to the entities wherein the promoters/directors of ZIL had substantial stake/control and such fund diversion was *prim facie* to defraud the shareholders.

63. As discussed hereinabove, the directions in the *interim order* do not stipulate compensation to the shareholders of ZIL who might have incurred loss due to price fall in the scrip of ZIL. It also does not contemplate compensation to the FCCB holders. Rather, it intends to compensate ZIL, should SEBI deem it necessary. The bank guarantee stipulated in para 25(ii) of the *interim order* is for the amount of sale proceeds of MSD business that was *prima facie* found during the preliminary inquiry to have been fraudulently diverted. It is not for the amount of loss that the investors trading in the scrip of ZIL might have incurred on account of price fall in the scrip after default in this case came to the light. I further note that apart from loss to the investors on account of price fall , the matter in issue in the present case has fraudulent asset stripping which has bearing on the fiduciary duties of the management vis-à-vis other non-promoter shareholders of ZIL whose value is *prima facie* found to have been eroded on account of diversion of the sale proceeds of MSD business leaving the liability of ZIL intact and putting financial burden on the shareholders. In this regard, the *interim order* does not distinguish between the institutional non-promoter shareholder and retail shareholders as sought to be contended by the noticees. I, therefore, do not find any merit in the contentions of the noticees in this regard.

64. In view of the above, I find that the noticees have not been able to make out a *prima facie* case for revocation or modification of the *interim order* and the material available on record justifies the continuation of the directions passed against them under the *ad interim ex-parte order* dated March 25, 2013.

65. I further note that the aforesaid acts and omissions on the part of the promoters/directors and the consequences thereof also raise the concerns about the non-observance of the principles of corporate governance as *prima facie* found in the *interim order*. I note that the directors are entrusted with the responsibility to take decisions for the company which is for the welfare of the company and its shareholders. I further note that true, fair, adequate and timely disclosures by the company form one of the basic tenets of governance in the listed companies and are essential for maintaining the integrity of the securities market. In this case, the promoters/directors have not only failed to observe their fiduciary duties to ensure equal treatment of shareholders of ZIL but also actively concealed the actual fact, made false, misleading and distorted disclosures as a device to defraud them as *prima* facie found in the *interim order*.

66. In the facts and circumstances of this case, I am of the view that the *prima facie* findings and directions in the *interim order* are in proportion to the alleged violations. In this regard, the observations of the Hon'ble Supreme Court, as a word of caution, in the matter of *N. Narayanan vs. Adjudicating Officer, SEBI,* in Civil Appeal Nos. 4112-4113 of 2013, (order dated April 26, 2013) is worth mentioning:

> *"A word of caution:*
> *43. SEBI, the market regulator, has to deal sternly with companies and their Directors indulging in manipulative and deceptive devices, insider trading etc. or else they will be failing in their duty to promote orderly and healthy growth of the Securities market. Economic offence, people of this country should know, is a serious crime which, if not properly dealt with, as it should be, will affect not only country's economic growth, but also slow the inflow of foreign investment by genuine investors and also casts a slur on India's securities market. Message should go that our country will not tolerate "market abuse" and that we are governed by the "Rule of Law". Fraud, deceit, artificiality, SEBI should ensure, have no place in the securities market of this country and 'market security' is our motto. People with power and money and in management of the companies, unfortunately often command more respect in our society than the subscribers and investors in their companies. Companies are thriving with investors' contributions but they are a divided lot. SEBI has, therefore, a duty to protect investors individual and collective, against opportunistic behavior of Directors and Insiders of the listed companies so as to safeguard market's integrity."*

67. In the light of above facts and circumstances, I, therefore, am of the considered view that no intervention is called for, at this stage, in either vacating the *interim* directions or modifying it, with respect to the noticees. I, therefore, in exercise of the powers conferred upon me under section 19 of the SEBI Act, read with sections 11(1), 11(4) and 11B thereof and section 12A of the SCRA hereby confirm the directions issued vide the *ad interim ex-parte order* dated March 25, 2013 against the noticees. Considering the submissions of the noticees that being the resident Indians they can purchase foreign exchange up to only USD 200,000 under Liberalized Remittance Scheme, I hereby give liberty to them to furnish bank guarantee for an amount equivalent to USD 33.93 million in Indian rupees.

68. This order shall remain in force till further directions.

DATE: April 11th, 2014 **RAJEEV KUMAR AGARWAL**
PLACE: MUMBAI **WHOLE TIME MEMBER**
SECURITIES AND EXCHANGE BOARD OF INDIA