BEFORE THE ADJUDICATING OFFICER

SECURITIES AND EXCHANGE BOARD OF INDIA

[ADJUDICATION ORDER NO.ISD/SGPL/FDIL/AO/DRK/AKS/EAD-3/295/61-11]

UNDER SECTION 15 I OF SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 READ WITH RULE 5(1) OF SECURITIES AND EXCHANGE BOARD OF INDIA (PROCEDURE FOR HOLDING INQUIRY AND IMPOSING PENALTIES BY ADJUDICATING OFFICER) RULES, 1995

Against:

Sethia Gems Pvt. Ltd.
72, New Hanuman Building
3rd Floor, Lamington Road
Grant Road, Mumbai - 400007
PAN No. AAHCS4460J

FACTS IN BRIEF

1. An alert was generated at IMSS regarding huge off-market transfer at National Securities Depository Ltd. (hereinafter referred to as '**NSDL**') and Central Depository Services (India) Ltd. (hereinafter referred to as '**CDSL**') wherein it was observed that significant quantity of shares of Flawless Diamond (India) Ltd. (hereinafter referred to as ' **FDIL** / **Company**') has been transferred through off-market transfer from Promoter / Non-Promoter related entities to Rotomac Global Private Ltd (hereinafter referred to as '**RGPL**') on 30/10/2009 and 31/10/2009.

2. Based on the alert, information was collected from Bombay Stock Exchange Ltd. (hereinafter referred to as '**BSE**'), NSDL and CDSL and clarification was sought from the company and RGPL.

APPOINTMENT OF ADJUDICATING OFFICER

3. I was appointed as the Adjudicating Officer and the same was communicated vide proceedings of the Whole Time Member appointing Adjudicating Officer dated 09.05.2011 under Section 15 I of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as '**SEBI Act**') read with Rule 3 of SEBI (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules, 1995 (hereinafter referred to as 'Rules') to inquire into and adjudge under Section 15A (b) of the SEBI Act, the violation of Regulations 13 (1), 13 (3) read with 13 (5) of the SEBI (Prohibition of Insider Trading) Regulations, 1992 (hereinafter referred to as '**PIT Regulations**') and Regulations 7 (1), read with 7 (2) of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (hereinafter referred to as '**Takeover Regulations**') alleged to have been committed by Sethia Gems Pvt. Ltd. (hereinafter referred to as '**noticee'**).

SHOW CAUSE NOTICE, HEARING AND REPLY

4. A Show Cause Notice No. A&E/DRK/AKS/20766/2011 (herein after referred to as **'SCN'**) dated 28.06.2011 was sent to the noticee by "Hand Delivery Acknowledgement Due" in terms of the provisions of Rule 4 of the SEBI (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules, 1995 requiring it to show cause as to why an inquiry should not be held against it and why penalty, if any, should not be imposed on it under Section 15A (b) of the SEBI Act.

5. However, the said notice came back undelivered with remark “office closed”. Vide letter dated 01.07.2011 the SCN was served through “Registered Post Acknowledgement Due”. In the said notice, it was alleged as follows:
   a. From the investigation report it is observed that noticee had offloaded 10,00,000 shares (6% of the paid up share capital of the company) to RGPL on 30.10.2009. After the transfer of the shares, noticee’s holding in FDIL had become zero. It is alleged that no disclosure has been made by the noticee for such transfer as required under PIT Regulations to the company which has led to the violation of Regulation 13 (3) read with Regulation 13 (5) of PIT Regulations.
   b. It was further observed that the transferred shares of FDIL have been transferred back to the noticee on 15.03.2010 by RGPL. It is alleged that the noticee had not disclosed his acquisition of shares of FDIL to the company and to the stock exchange as required under Regulations 7 (1) read with 7 (2) of Takeover Regulations.
   c. Further, it is observed that under Regulation 13 (1) of PIT Regulations, noticee was required to disclose to the company within 2 working days of the receipt of intimation of allotment of shares or the acquisition of shares, as the case may be. However, it is alleged that no disclosure for such acquisition of shares has been made by the noticee to the company as required under PIT Regulations.

6. Vide personal hearing notice dated 04.08.2011, the noticee was granted time till 12.08.2011 to submit a detailed reply to the SCN and attend the hearing on 22.08.2011 at SEBI Bhavan, Mumbai. The said hearing notice was sent through “Registered Post Acknowledgement Due”. However the noticee failed to attend the scheduled hearing without furnishing any reasons.

7. Thereafter a final hearing notice dated 26.08.2011 was sent to the noticee by "Registered Post Acknowledgement Due" granting time till 05.09.2011 to submit a detailed reply to the SCN and attend the hearing on 08.09.2011 at SEBI Bhavan, Mumbai. The said hearing notice came back undelivered with remark "unclaimed". Subsequently another hearing notice dated 26.09.2011 along with the first two hearing notices were affixed at the noticee's address on 28.09.2011. The last hearing notice granted noticee time till 05.10.2011 to submit a detailed reply to the SCN and attend the hearing on 11.10.2011 at SEBI Bhavan, Mumbai. The hearing notice dated 26.09.2011 was also uploaded at the SEBI website under the heading "unserved summons / notices" and was also sent by "Registered Post Acknowledgement Due" but it came back undelivered with remark "door closed".
8. In response to the last hearing notice, noticee vide its letter dated 04.10.2011 authorized Shri Balveer Singh Choudhary, Chartered Accountant (hereinafter referred to as '**AR**') to attend the scheduled hearing. During the personal hearing the AR undertook to submit a detailed reply to the SCN within a week from the date of hearing.
9. However, the noticee vide its letter dated 07.11.2011 which was received by SEBI on 14.11.2011 submitted a reply to the SCN wherein it stated as follows-
    - The noticee submitted that it had not offloaded 10,00,000 shares to RGPL on 31st October 2009 but these shares were given to RGPL as loan for the purpose to create margin to stock broker. Since it had not sold any equity shares of FDIL therefore there was no need to file the disclosure under Regulation 13(3) read with Regulation 13(5) of the PIT Regulations.
    - As per the Regulation 13(3) read with Regulation 13(5) (b) disclosure is to be filed when the acquisition or sale of shares or voting rights, as the case may be. In the instant case the noticee had given loan not sale/ offloaded the aforesaid shares, therefore the same is not covered under Regulation 13(5) of PIT Regulations.
    - Further, it is submitted that the loan shares of FDIL have been transferred back to the noticee on 15th March 2010 and the transaction is completed. As the said shares were returned back as per the loan

agreement therefore the said transaction is not covered under Regulation 7(1) read with Regulation 7(2) of Takeover Regulations. Similarly the said transaction is not covered under Regulation 13(1) of the PIT Regulations.

CONSIDERATION OF EVIDENCE AND FINDINGS

10. I have taken into consideration the facts and circumstances of the case and the material made available on record. The allegations in the present matter are that the noticee offloaded 10,00,000 shares of FDIL on 30.10.2009 to RGPL and the same number of shares were transferred back to the noticee by RGPL on 15.03.2010 but it failed to make disclosures under Takeover Regulations and PIT Regulations.
11. The noticee has submitted that it had entered into a pledge agreement with RGPL for 10,00,000 shares. However, the investigation report observes that the documents submitted for the proof of the pledge are not in accordance with the provisions of Depositories Act, 1996, SEBI (Depositories and Participants) Regulations, 1996 and the Bye-laws and Business Rules of the Depositories. Pledge or hypothecation under the Depository Regulations does not involve any transfer of shares from the pledger to the pledgee as only an entry is recorded in respect of the securities so pledged or hypothecated, which would evidence the creation of pledge. Since shares from the noticee were clearly transferred in off-market to RGPL and RGPL's demat account does not indicate any creation of pledge, the investigation report observes that the noticee's argument regarding shares were pledged to RGPL may not be accepted.
12. In this regard it may be noted that the said shares of FDIL are in demat form. The manner of creating pledge is given in the Depositories Act, 1996 and SEBI (Depositories and Participants) Regulations, 1996. It is observed from Section 12 of the Depositories Act, 1996 and Regulation 58 of SEBI (Depositories and Participants) Regulations, 1996 that for creation of

pledge, the pledger has to make an application to the depository through the participant and the participant after making a note in its records of the notice of pledge, forward the application to the depository. The depository after confirmation from the pledgee that the securities are available for pledge with the pledger shall within 15 days of receipt of the application creates and records the pledge and send an intimation of the same to the participants of the pledger and the pledgee. On receipt of the intimation the participants of both the pledger and the pledgee shall inform the pledger and the pledgee respectively of the entry of creation of the pledge. An entry in the records of a depository shall be evidence of a pledge.

13. Further, it is also seen from Bye-Law 9.9 of NSDL and Business Rule 12.9 of NSDL that there is a specific procedure for creation of pledge. The pledger has to submit an instruction to the depository participant to initiate a pledge request in the DPM (software provided by NSDL to the depository participant) indicating the option 'create a pledge' in the pledge form. The depository participant will accept the form for processing and issue an acknowledgment for the same to the pledger. The depository participant then will enter the details of the request in the DPM, generate a pledge instruction number for the request and release the request to NSDL. The securities pledged are moved from 'Free balances' to 'Pledged balances' account. The depository participant shall write the pledge instruction number on the pledge form and intimate the same to the pledger. Further, Regulations 58 (6) and 58 (7) of SEBI (Depositories and Participants) Regulations, 1996 lays down the manner of cancellation of a pledge. It states that a pledge may be cancelled by the depository if the pledger or the pledgee makes an application to the depository through its participant provided there is prior concurrence of the pledgee. The depository on the cancellation of the entry of pledge shall inform the participant of the pledger.

14. It is noted from the available records that none of the documents required under Depositories Act, 1996, SEBI (Depositories and Participants) Regulations, 1996, Bye-Law and Business Rule of NSDL as discussed above for creation of pledge such as copy of the instruction to the depository participant given by the pledger to initiate a pledge request or the acknowledgment by the depository participant for processing pledgee's request or pledge instruction number, etc. has not been submitted by the noticee. Rather it is seen from the transaction statements received from NSDL that on 30/10/2009, noticee had transferred in an off-market transaction 10,00,000 shares of FDIL to RGPL. Further, NSDL in its letter dated 03.06.2010 has submitted data for the period from 16.10.2001 to 26.05.2010 regarding creation of pledge in the scrip of FDIL. It is observed from the said data that the noticee has not created any pledge in the scrip of FDIL in favour of RGPL as claimed by the noticee. Further, the noticee has also not submitted a copy of the application made to the depository through its participant to cancel the pledge. Thus, it can be observed from the above that the noticee has not followed the procedure prescribed under the Depositories Act and the Regulations framed thereunder for pledging of shares or for cancellation of the pledge.

15. In this case, I would like to quote the order of the Hon'ble Securities Appellate Tribunal, in *Parsoli Corporation Limited et al* Vs *SEBI* dated 12.08.2011 wherein it was held as follows:

> *"…There is no material on the record to show that the shares were ever pledged. The mere ipse dixit of the appellants cannot be accepted. It is pertinent to mention that there is a procedure prescribed under the Depositories Act and the regulations framed thereunder for pledging shares and when a pledge is created the same is recorded in the records of the depository. Had a pledge been created, as is now sought to be argued, the appellants would have produced the records from the depository..."*

16. In view of the facts of the case and the Order of the Hon'ble Securities Appellate Tribunal discussed in pre para, noticee's submission that the shares were pledged is not acceptable.

17. The investigation report states that the noticee had offloaded 10,00,000 shares (6% of the paid up share capital of the company) in off-market to RGPL on 30.10.2009 and after the transfer of the shares, noticee's holding in FDIL had become zero. The said 10,00,000 shares of FDIL were credited to the account of RGPL on the same day. There is nothing on record to show that the noticee had made disclosure about the aforesaid transfer as required under Regulation 13 (3) read with Regulation 13 (5) of PIT Regulations to the company. Noticee's argument that there is no need to file any disclosure for pledge of shares under PIT Regulations is not acceptable as the shares were not pledged as concluded above. Thus, it can be concluded that noticee has violated Regulation 13 (3) read with Regulation 13 (5) of PIT Regulations. The text of the said Regulations is reproduced below:

SEBI (Prohibition of Insider Trading) Regulations, 1992
Continual disclosure.

13 (3) Any person who holds more than 5% shares for voting rights in any listed company shall disclose to the company in Form C the number of shares or voting rights held and change in shareholding or voting rights, even if such change results in shareholding falling below 5%, if there has been change in such holdings from the last disclosure made under sub-regulation (1) or under this sub-regulation; and such change exceeds 2% of total shareholding or voting rights in the company.

13 (5) The disclosure mentioned in sub-regulations (3) and (4) shall be made within two working days of:

(a) the receipts of intimation of allotment of shares, or

(b) the acquisition or sale of shares or voting rights, as the case may be.

18. Further the investigation report observes that the transferred shares of FDIL were transferred back to the noticee on 15.03.2010 by RGPL. The SCN

alleges that noticee has not made disclosure about the acquisition of shares of FDIL to the company and to the stock exchange under Regulations 7 (1) read with 7 (2) of Takeover Regulations and under Regulation 13 (1) of PIT Regulations to the company. The noticee's argument that the said shares were returned as per the loan / pledge agreement and therefore there was no need to make disclosure is not acceptable as the shares were not pledged as concluded above. Thus, it can also be concluded that noticee has violated Regulations 7 (1) read with 7 (2) of Takeover Regulations and Regulation 13 (1) of PIT Regulations. The text of the said Regulations is reproduced below:

SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997

Acquisition of 5 per cent and more shares or voting rights of a company.

7. (1) Any acquirer, who acquires shares or voting rights which (taken together with shares or voting rights, if any, held by him) would entitle him to more than five per cent or ten per cent or fourteen per cent or fifty four per cent or seventy four per cent shares or voting rights in a company, in any manner whatsoever, shall disclose at every stage the aggregate of his shareholding or voting rights in that company to the company and to the stock exchanges where shares of the target company are listed.

…

(2) The disclosures mentioned in sub-regulations (1) and (1A) shall be made within two days of,—

(a) the receipt of intimation of allotment of shares; or

(b) the acquisition of shares or voting rights, as the case may be.

SEBI (Prohibition of Insider Trading) Regulations, 1992

Disclosure of interest or holding by directors and officers and substantial shareholders in a listed companies - Initial Disclosure.

13. (1) Any person who holds more than 5% shares or voting rights in any listed company shall disclose to the company in Form A, the number of shares or voting rights held by such person, on becoming such holder, within 2 working days of :—

(a) the receipt of intimation of allotment of shares; or

(b) the acquisition of shares or voting rights, as the case may be.

19. The said violations attract penalty under Section 15A (b) of the SEBI Act. The text of Section 15A (b) is as follows:

> 15A. Penalty for failure to furnish information, return, etc.- If any person, who is required under this Act or any rules or regulations made thereunder,-
>
> …
>
> (b) to file any return or furnish any information, books or other documents within the time specified therefor in the regulations, fails to file return or furnish the same within the time specified therefor in the regulations, he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

20. In this regard, the provisions of Section 15J of the SEBI Act and Rule 5 of the Rules require that while adjudging the quantum of penalty, the adjudicating officer shall have due regard to the following factors namely;

a. the amount of disproportionate gain or unfair advantage wherever quantifiable, made as a result of the default
b. the amount of loss caused to an investor or group of investors as a result of the default
c. the repetitive nature of the default

21. It has been noted from the material available on record that it is difficult to quantify any gain or unfair advantage accrued to the noticee as a result of this kind of default committed by the noticee. The investigation report has also not quantified the profit/ loss for the nature of violations committed by the noticee and no material is made available on record to assess the disproportionate gain or unfair advantage and amount of loss caused to an investor or group of investors as a result of actions of the noticee.

22. In view of the abovementioned conclusion and after considering the factors under Section 15J of the SEBI Act, I hereby impose a penalty of

₹ 2,00,000/- (Rupees Two Lakh only) on the noticee under Section 15A (b) of the Securities and Exchange Board of India Act, 1992 for the violations of Regulation 13 (1), Regulation 13 (3) read with Regulation 13 (5) of SEBI (Prohibition of Insider Trading) Regulations, 1992 and ₹ 1,00,000/- (Rupees One Lakh only) for the violation of Regulations 7 (1) read with 7 (2) of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 which is appropriate in the facts and circumstances of the case.

ORDER

23. In exercise of the powers conferred under Section 15 I of the Securities and Exchange Board of India Act, 1992, and Rule 5 of Securities and Exchange Board of India (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules, 1995, I hereby impose a consolidated penalty of ₹ 3,00,000/- (Rupees Three Lakh only) on Sethia Gems Pvt. Ltd. having PAN No. AAHCS4460J in terms of the provisions of Section 15A (b) of the Securities and Exchange Board of India Act, 1992 for the violations of Regulations 7 (1) read with 7 (2) of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 and Regulation 13 (1), Regulation 13 (3) read with Regulation 13 (5) of SEBI (Prohibition of Insider Trading) Regulations, 1992. In the facts and circumstances of the case, I am of the view that the said penalty is commensurate with the violations committed by the noticee.

24. The penalty shall be paid by way of Demand Draft drawn in favour of “SEBI – Penalties Remittable to Government of India” payable at Mumbai within 45 days of receipt of this order. The said demand draft shall be forwarded to Deputy General Manager- ISD, Securities and Exchange Board of India, Plot No. C4-A, ‘G’ Block, Bandra Kurla Complex, Bandra (E), Mumbai – 400051.

25. In terms of the provisions of Rule 6 of the Securities and Exchange Board of India (Procedure for Holding Inquiry and Imposing Penalties by Adjudicating Officer) Rules 1995, copies of this order are being sent to Sethia Gems Pvt. Ltd. having its office at 72, New Hanuman Building, 3rd Floor, Lamington Road, Grant Road, Mumbai- 400007 and also to the Securities and Exchange Board of India, Mumbai.

Place: Mumbai

Date: November 23, 2011

D. RAVI KUMAR
CHIEF GENERAL MANAGER &
ADJUDICATING OFFICER