BEFORE THE ADJUDICATING OFFICER

SECURITIES AND EXCHANGE BOARD OF INDIA

[ADJUDICATION ORDER NO. VSS/AO- 14/2009]

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

In respect of

Dr. K Koteswara Rao

(PAN. AHOPK5487E)

FACTS OF THE CASE IN BRIEF

1. The shares of Transgene Biotek Limited (hereinafter referred to as **"TBL/company"**) are listed on Bombay Stock Exchange (hereinafter referred to as **"BSE"**). Securities and Exchange Board of India (hereinafter referred to as "**SEBI**") conducted an investigation into the trading of shares of TBL from the period November 26, 2005 to December 21, 2005 (hereinafter referred to as "**investigation period**"). Pursuant to the investigation, it was alleged that Dr K Koteswara Rao, Promoter cum Chairman and Managing Director of TBL, had failed to make necessary disclosure under regulations 13(4) and 13(5) of SEBI (Prohibition of Insider Trading) Regulations, 1992 (hereinafter referred to as **"PIT")** with regard to sale of 1,50,000 shares. It was also alleged that Dr. K Koteswara Rao had made disclosure under regulations 7(1A) and 7(2) of SEBI (Substantial Acquisition of Shares and Takeovers)

Regulations, 1997 (hereinafter referred to as **"SAST"**) with regard to his acquisition of 11,12,000 shares (7.40% of the paid-up capital of TBL) from his son Mr. K Srinivas through off-market in June 2006 on July 5, 2006, which is allegedly not in compliance with the said regulations. It was also alleged that Dr. K Koteswara Rao had failed to make a public announcement under regulation 11(1) of SAST with regard to his acquisition of 11,12,000 shares (7.40% of the paid-up capital of TBL) from his son Mr. K Srinivas through off-market in June 2006. Consequently, it was alleged that he was liable for penalty under sections 15A(b) and 15H of Securities and Exchange Board of India Act, 1992 (hereinafter referred to as "**SEBI Act**").

APPOINTMENT OF ADJUDICATING OFFICER

2. The undersigned was appointed as Adjudicating Officer vide order dated July 17, 2008 under section 15 I of 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 the alleged violations of provisions of the aforesaid regulations.

SHOW CAUSE NOTICE, HEARING AND REPLY

3. Show Cause Notice No. EAD-5/VSS/JR/137842/2008 dated September 16, 2008 (hereinafter referred to as **"SCN"**) was issued to Dr K Koteswara Rao (hereinafter referred to as **"Noticee"**) under rule 4(1) of the Rules to show cause as to why an inquiry should not be held against the Noticee and penalty be not imposed on him under sections 15A(b) and 15H of SEBI Act for the alleged violations specified in the said SCN.

4. The Noticee vide letter dated October 29, 2008 replied to the SCN and also sought personal hearing in the matter.

5. In the interest of natural justice and in order to conduct an inquiry as per rule 4 (3) of the Rules, the Noticee was granted an opportunity of personal hearing on December 11, 2008 at SEBI, Southern Regional Office, Chennai vide notice dated November 24, 2008. The Noticee was also advised to furnish details of his compliance with disclosure requirements u/r 6, 7 and 8 of SAST. Mr. S S Marthi, Authorized Representative, (hereinafter referred to as "**AR**") appeared. During the hearing, the AR reiterated the submissions made vide letter dated October 29, 2008. He also furnished the details sought from the Noticee.

CONSIDERATION OF ISSUES AND FINDINGS

6. The issues that arise for consideration in the present case are :

a) Whether the Noticee had violated regulations 13(4) read with 13(5) of PIT and 7(1A) read with 7(2) of SAST?

b) Does the violation/s, if any, on the part of the Noticee attract monetary penalty under section 15A(b) of SEBI Act?

c) Whether the Noticee had violated regulation 11(1) of SAST?

d) Does the violation, if any, on the part of the Noticee attract monetary penalty under section 15H of SEBI Act?

e) If so, what would be the monetary penalty that can be imposed taking into consideration the factors mentioned in section 15J of SEBI Act?

7. Before moving forward, it is pertinent to refer to the provisions of regulations 13(4) and 13 (5) of PIT and 7 (1A), 7(2) and 11(1) of SAST, sections 15A(b), 15H and 15J of SEBI Act which reads as under:

> *13(4) Any person who is a director or officer of a listed company, shall disclose to the company in Form D, the total number of shares or voting rights held and change in shareholding or voting rights, if there has been a change in such holdings from the last disclosure made under sub-regulation (2) or under this sub-regulation, and the change exceeds Rs. 5 lakh in value or 25,000 shares or 1% of total shareholding or voting rights, whichever is lower.*
>
> *13(5) The disclosure mentioned in sub-regulations (3) and (4) shall be made within 4 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.*
>
> *7(1A) Any acquirer who has acquired shares or voting rights of a company under sub-regulation (1) of regulation 11, shall disclose purchase or sale aggregating two per cent or more of the share capital of the target company to the target company, and the stock exchanges where shares of the target company are listed within two days of such purchase or sale along with the aggregate shareholding after such acquisition or sale.*
>
> *7(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.*

Consolidation of holdings

11. (1) No acquirer who, together with persons acting in concert with him, has acquired, in accordance with the provisions of law, 15 per cent or more but less than fifty five per cent (55%) of the shares or voting rights in a company, shall acquire, either by himself or through or with persons acting in concert with him, additional shares or voting rights entitling him to exercise more than 5 per cent of the voting rights, in any financial year ending on 31st March unless such acquirer makes a public announcement to acquire shares in accordance with the regulations.

Penalty for failure to furnish information, return, etc.

15A. If any person, who is required under this Act or any rules or regulations made thereunder,-

(a) ….

(b) To file any return or furnish any information, books or other documents within the time specified therefore in the regulations, fails to file return furnish the same within the time specified therefore 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];

Penalty for non-disclosure of acquisition of shares and takeovers

15H. If any person, who is required under this Act or any rules or regulations made thereunder, fails to,

(i) disclose the aggregate of his shareholding in the body corporate before he acquires any shares of that body corporate; or

(ii) make a public announcement to acquire shares at a minimum price; or

(iii) make a public offer by sending letter of offer to the shareholders of the concerned company; or

(iv) make payment of consideration to the shareholders who sold their shares pursuant to letter of offer,

he shall be liable to a penalty of twenty five crore rupees or three times the amount of profits, made out of such failure, whichever is higher.

15J - Factors to be taken into account by the adjudicating officer

While adjudging quantum of penalty under section 15-I, 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.

8. As regards the allegation of violation of regulations 13(4) and 13(5) of PIT, I find that the same has been made on the premise that the Noticee had sold 1,50,000 shares constituting 0.9987% of the paid up capital of TBL. On perusal of the submissions of the Noticee and other documents forwarded by him along with his submissions, I have noted the following:

- During 1995, the promoters of TBL pledged shares with various entities from whom loans were raised by TBL. One of such entities from whom money was borrowed was Ankit Tradesec Limited (hereinafter referred to as "**Ankit/pledgee**"). As part of the collateral, the promoters of TBL pledged 8,30,000 shares with Ankit which included 1,50,000 shares of the Noticee referred to above. Due to financial crisis, TBL defaulted in the repayment of debt and consequently, Ankit invoked the pledge and sold some of the pledged shares. The sale of shares by Ankit was done without the consent of the pledgors. With the result, legal dispute started between the parties to the transaction.
- After a prolonged litigation, a compromise settlement was arrived at to settle the disputes amicably. The same had been filed in the respective Courts, where several suits/cases were pending including S.C. Suit No. 1929 of 2002 in the Bombay

City Civil Court. The settlement of dispute was intimated to BSE vide letter dated March 11, 2003.

- Clause 11 of the Memorandum of Settlement dated February 21, 2003 between the pledgee and TBL states as under:

"*TBL agree, confirm and declare and undertake that they shall effect registration and transfer of the said pledged shares as per provisions of law in the following manner;*

(a) TBL group undertakes that such of the said pledged shares as have been lodged/ delivered to TBL for effecting transfer thereof, till date and those shares which shall be lodged/ delivered for transfer, on or before the date of withdrawal and/ or dismissal of the last of the ATL proceedings mentioned above, shall be transferred in accordance with the provisions of law, by TBL in favour of the transferees mentioned therein, within a period of 60 days of the withdrawal and/ or dismissal of all the aforesaid proceedings.

(b) Such of the said pledged shares as shall be lodged/ delivered to TBL for effecting registration and transfer thereof, after the withdrawal and/ or dismissal of all the aforesaid proceedings filed by the ATL group against the TBL group, shall be transferred in accordance with law by TBL to the transferees mentioned therein."

- When the dispute was pending, Ankit sold some of the shares pledged by the promoters of TBL with it. The shares so sold included the 1,50,000 shares pledged by the Noticee. Thus, the sale was effected by the pledgee and not by the Noticee. With the said sale of shares, the Noticee did not gain anything since the consideration of the said sale did not accrue to him.

- TBL vide letter dated June 23, 1999 informed BSE with regard to the shares pledged with various entities as per the agreement entered into with them.

S. No	Name of the Entity	No. of Shares
1.	Ankit Tradesec Limited	5,00,000
2.	Nitin Kumar Didwania	3,00,000
3.	T.C.I. Finance Limited	5,58,793
4.	A.S Leasing and Finance Limited	1,25,000

- A copy of the said agreement/s was also forwarded to BSE vide letter dated June 23, 1999. The details of the shareholding pattern of the company were also disclosed to BSE vide the said letter.

Category	Percentage
Promoters	19.83
Bodies Corporate	3.06
Public	77.11

9. I find from the above submissions of the Noticee that when TBL defaulted in the repayment of debt, the pledgees (which included Ankit with whom 1,50,000 shares of the Noticee was pledged) sold some of the pledged shares. As these shares were in physical mode, they were lodged for transfer by the buyers of those shares as and when the book closure of TBL was announced. This finding is supported by the statement made by TBL to BSE vide letter dated September 20, 1999 that '*the company has already transferred 4,22,000 shares received for transfer out of the pledged shares*.' I also find from the submissions of the Noticee that the shares belonging to him which were pledged had come for transfer in the year 2005, i.e. after a lapse of around 9 years. This has also been mentioned in the investigation report of SEBI. I also find that the trading in the scrip of TBL was suspended during 1996-2001 and probably due to this suspension in trading, the shares were not lodged for transfer earlier.

10. From the above, I find that the Noticee came to know of the sale of his shares when the same were lodged for transfer and the transfer was effected by TBL during June to December 2005. The Noticee could have made necessary disclosures under PIT, atleast at this point of time. There is nothing on record to show that the Noticee had done the same. Therefore, the allegation of failure to comply with the provisions of regulation 13(4) read with 13(5) of PIT stands established.

11. There is no material available on record to indicate any disproportionate gain or unfair advantage or amount of loss caused to an investor or group of investors and also the repetitive nature of the default on the part of the Noticee. On the other hand, I find that the Noticee had not received any consideration in respect of the sale of his shares as the sale was effected by Ankit due to the default of TBL. Further, in view of the unusual circumstances and other mitigating factors stated above, I am of the view that the violation does not warrant imposition of any monetary penalty.

12. As regards the acquisition of 11,12,000 shares by the Noticee from his son in June, 2006 I find that the Noticee had acquired these shares on June 28, 2006 but made the disclosure in terms of regulation 7(1A) read with 7(2) of SAST on July 5, 2006. In terms of the provisions of the said regulations, the disclosure was ought to have been made within 2 days of acquisition i.e. on or before June 30, 2006 in the instant case. However, the disclosure was made on July 5, 2006, i.e. with a delay of 5 days. The Noticee has not disputed this.

13. However, the Noticee has contended, inter alia, that the said acquisition did not attract the provisions of the said regulations in view of the following :

(a) The transfer had taken place within the family to facilitate certain family issues.
(b) The relationship between the transferor and transferee is that of father and son in this case. There was no consideration in buying or selling these shares between them due to the relationship.
(c) No single share out of the said 11,12,000 shares has been sold till date.
(d) There had been neither any change in the percentage of shareholding of the family since the transfer of the said shares nor was there any sort of gain till this day on that said transfer of shares.
(e) As per regulation 7(1A) of SAST, an acquisition has to be by way of a purchase or sale of shares. In this case, there had been no purchase or sale of shares since it was a transfer consequent to a family settlement and also without any overall gain or loss either in the percentage of shareholding or in any other form of gain or loss to the transferor and transferee. A purchase or a sale necessarily follows payment of consideration, whereas in this case there had never been such a consideration.

14. I have noted the aforesaid submissions of the Noticee. I find that the contention of the Noticee is contradictory in nature. On the one hand, the Noticee has contended that the acquisition of 11,12,000 shares from his son had not attracted the provisions of regulation 7(1A) and on the other hand, I find that the Noticee had made the

disclosure on July 5, 2006. If the provisions of SAST were not attracted, the Noticee ought not to have made the disclosure in the first instance. However, the Noticee had made the disclosure. But when he has been charged for delayed disclosure, he is now questioning the applicability of the provisions. I am of the view that it is an afterthought and therefore, hold that the submissions of the Noticee in this regard are devoid of any merit.

15. In terms of regulations 7(1A) and 7(2) of SAST, any acquirer (who is covered under regulation 11(1) of SAST) who acquires shares or voting rights aggregating to 2% or more is required to inform the target company and the stock exchange/s where the shares of the company are listed. The stock exchange/s, in turn, has to disseminate this information to the public. Timely disclosure of this vital information sets the benchmark in terms of particulars of shareholders holding significant stake including the changes in their shareholding for the information of the general public. The Noticee, therefore, was under obligation to make the disclosure within the time specified in the respective regulations. I find from the submissions of the Noticee that he has admitted the delay in making the disclosure under regulations 7(1A) and 7(2) of SAST but defended the same by citing certain reasons stated above. I am of the view that the reasons cited by the Noticee, did not, in any way absolve him of his failure to comply with the statutory requirements on time. At best, these could be considered as mitigating factors while quantifying the penalty.

16. By not making the disclosure on time, the Noticee failed to comply with his statutory obligation. The timely disclosure is mandated for the benefit of the investors at large. In Appeal No. 66 of 2003 - *Milan Mahendra Securities Pvt. Ltd. Vs SEBI* – Order dated April

15,2005 the Hon'ble SAT has observed that, *"the purpose of these disclosures is to bring about transparency in the transactions and assist the Regulator to effectively monitor the transactions in the market."* Though it may not be possible to ascertain the exact monetary loss to the investors on account of default by the Noticee, the change in the shareholding of the Noticee and timely disclosure thereof, were of some importance from the point of view of outside shareholders/other investors as that would have prompted them to buy or sell shares of TBL. It would, however, be difficult to come to a firm conclusion as to how the general shareholders would have reacted on knowing the aforesaid change in the shareholding of the Noticee. The Noticee could not pre-judge the reaction of the investors. By virtue of the failure on the part of the Noticee to make the necessary disclosure on time, the fact remains that the shareholders/investors were deprived of the important information at the relevant point of time.

17. The Hon'ble Supreme Court of India in the matter of *SEBI Vs. Shri Ram Mutual Fund* [2006] 68 SCL 216(SC) held that "*once the violation of statutory regulations is established, imposition of penalty becomes sine qua non of violation and the intention of parties committing such violation becomes totally irrelevant. Once the contravention is established, then the penalty is to follow"*.

18. I also note that in the case of P.K. Tayal Vs. SEBI (Appeal No. 89 of 2007), the Hon'ble SAT upheld a penalty of Rs.1 lakh on the appellant for violation of regulations 7 (1) and 7 (2) of SAST. Also, in the matter of Mega Resources and Others Vs. SEBI, (Appeal No. 138/2003, 138 A to 138F/2003) the Hon'ble SAT reduced the penalty of Rs.3 lakhs to Rs.1.5 lakhs on seven entities for the violation of Regulation 7 (1) and 7 (2) of SAST.

19. From the material available on record, it is difficult to ascertain the disproportionate gain or unfair advantage to the Noticee which may have accrued due to the aforesaid failure. I do not find any material on record to establish repetitive nature of the default committed by the Noticee.

20. In view of the foregoing, I impose a penalty of Rs. 25,000/- (Rupees Twenty Five Thousand only) under section 15A (b) of the SEBI Act on the Noticee which will commensurate with violation committed by him.

21. With the acquisition of 11,12,000 shares (7.4%) on June 28, 2006, the shareholding of the Noticee had gone up from 34,30,202 shares (22.84%) to 45,42,202 shares (30.24%). As the acquisition exceeded the creeping acquisition limit of 5% specified u/r 11 (1) of SAST, the Noticee ought to have made a public announcement and complied with the provisions of SAST. As the Noticee failed to comply with the provisions of regulation 11(1) of SAST, it was alleged that he had violated the said regulation.

22. The Noticee has contended, inter-alia, that the acquisition is covered under regulation 3 (1)(e)(ii) of SAST, since the same was from his son and consequently, exempted from the applicability of regulation 11(1) of SAST.

23. On perusal of the provisions of regulation 3(1)(e)(ii) of SAST, I find that one of the conditions precedent, in order to avail the benefit of exemption under the said regulation, is compliance with the disclosure requirements specified under regulations 6, 7 and 8 of SAST by the acquirer and the transferee. In order to examine the

extent of compliance, the Noticee was advised vide notice dated November 24, 2008 to furnish the status of compliance with the provisions of regulations 6, 7 and 8 of SAST. The format in which the compliance report needs to be submitted was also forwarded to him along with the said notice. The Noticee vide letter dated December 8, 2008 submitted the status of compliance with the provisions of regulation 6, 7 and 8 of SAST which is as under:

Regulation/ Sub Regulation	Due Date for Compliances as mentioned in the regulations	Actual date of compliance	Delay, if any (in No of Days) Col.4-Col.3
6(1)	20.04.1997	17.08.2002	1942
6(3)	20.04.1997	17.08.2002	1942
8(1)	21.04.1998	04.03.2004	2138
8(2)	21.04.1998	04.03.2004	2138
8(1)	21.04.1999	04.03.2004	1773
8(2)	21.04.1999	04.03.2004	1773
8(1)	21.04.2000	04.03.2004	1408
8(2)	21.04.2000	04.03.2004	1408
8(1)	21.04.2001	04.03.2004	1043
8(2)	21.04.2001	04.03.2004	1043
8(1)	21.04.2002	17.08.2002	116
8(2)	21.04.2002	17.08.2002	116
8(1)	21.04.2003	19.05.2003	28
8(2)	21.04.2003	19.05.2003	28
8(1)	21.04.2004	07.04.2004	NIL
8(2)	21.04.2004	07.04.2004	NIL
8(1)	21.04.2005	05.04.2005	NIL
8(2)	21.04.2005	05.04.2005	NIL
8(1)	21.04.2006	12.04.2006	NIL
8(2)	21.04.2006	12.04.2006	NIL
7 (1) &(2)		17.08.2002	NIL
7 (1A) &(2)		17.08.2002	NIL

24. I find from the above that the disclosures have been made with delay. I am of the view that delayed compliance is as good as no compliance. As the condition precedent has not been fulfilled, the acquisition would not be eligible for exemption from the applicability of regulation 11(1) of SAST under regulation 3(1)(e)(ii) of SAST. The claim of the Noticee, therefore, is not acceptable.

25. Thus, the Noticee ought to have made a public announcement under regulation 11(1) of SAST. I find that the Noticee had failed to do so. Therefore, I hold that the allegation of violation of regulation 11(1) of SAST by the Noticee stands established.

26. It has been held by the Hon'ble SAT in the case of *Arya Holdings Limited Vs. P Sri Sai Ram, Adjudicating Officer*, -- Appeals No.3-5 of 2001 – Order dated May 04, 2001 – that *"……., the acquirer is required to comply with the requirement of making a public offer in terms of regulation 10, and failure to do so would attract the provisions of section 15H(ii)."* I, therefore, hold that the Noticee is liable for monetary penalty under section 15H(ii) of the SEBI Act as he had failed to comply with the requirements of making a Public Offer in terms of regulation 11(1) of SAST.

27. The Hon'ble Supreme Court of India in the matter of *SEBI Vs. Shri Ram Mutual Fund* [2006] 68 SCL 216(SC) held that "*once the violation of statutory regulations is established, imposition of penalty becomes sine qua non of violation and the intention of parties committing such violation becomes totally irrelevant. Once the contravention is established, then the penalty is to follow"*.

28. On perusal of the various provisions of SAST, it is observed that the open offer process includes appointment of a SEBI registered merchant banker as manager to the offer, determination of offer size and price, opening of an escrow account, making a public announcement in newspapers, filing of offer document with SEBI, dispatch of offer document to the eligible share holders, etc. By not having complied with the mandatory requirement of SAST, the Noticee has also avoided the expenditure which otherwise he would have incurred towards cost of engaging the services of a

Merchant Banker, making a public announcement in newspapers, filing of offer documents with SEBI, dispatch of offer documents to the eligible share holders, etc. To this extent also it can be said that the Noticee has earned disproportionate gain or unfair advantage. The Noticee failed to fulfill the statutory obligation of making the public announcement and with the result, denied the statutory right of the shareholders of TBL to exit through the open offer mechanism. To this extent, there was loss to the investors. I do not find any material on record to establish repetitive nature of the default committed by the Noticee.

29. I have considered the following submissions of the Noticee as mitigating factors while deciding the quantum of penalty :

(a) No consideration was involved in the transfer of said shares.

(b) The transfer was between son and father (Noticee), as part of family arrangement.

(c) As both, the acquirer/Noticee and the seller, belong to the promoter-group, the overall shareholding of the promoter-group remained unchanged.

(d) None of these shares has been sold in the market till date.

30. In view of the foregoing, I impose a penalty of Rs.1,00,000/- (Rupees One Lakh only) under section 15H (ii) of the SEBI Act on the Noticee which will be commensurate with the violation committed by him.

ORDER

31. The Noticee shall pay the total penalty of Rs.1,25,000/- (Rupees One Lakh Twenty Five Thousand only) {Rs.25,000/- under section 15A(b) and Rs.1,00,000/- under section 15H(ii)} by way of demand

draft 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 should be forwarded to Ms. Barnali Mukherjee, General Manager, Investigations Department, SEBI, SEBI Bhavan, Plot No. C – 4 A, “G” Block, Bandra Kurla Complex, Bandra (E), Mumbai – 400 051.

32. In terms of rule 6 of the Rules, copies of this order are sent to the Noticee and also to the Securities and Exchange Board of India.

Date: **February 06, 2009** **V.S.SUNDARESAN**

Place: **MUMBAI** **ADJUDICATING OFFICER**