BEFORE THE ADJUDICATING OFFICER

SECURITIES AND EXCHANGE BOARD OF INDIA

[ADJUDICATION ORDER NO. VSS/AO-10/2008]

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"**) and Hyderabad Stock Exchange (hereinafter referred to as **"HSE"**). SEBI conducted an investigation into the affairs relating to buying and selling and dealing in the shares of TBL. The investigation covered the period from November 26, 2005 to December 21, 2005. During the said investigation period, the shares of TBL got traded at BSE only.

2. The investigation conducted by SEBI revealed that Dr K Koteswara Rao (hereinafter referred to as **"Noticee"**), Promoter cum Chairman and Managing Director of TBL, had acquired 11,12,000 shares (7.40% of the paid-up capital) in June 2006 from his son Mr. K Srinivas through an off-market transaction. SEBI observed that the Noticee had informed about the said acquisition on July 5, 2006. It was alleged that the Noticee failed to make necessary disclosures on time,

    a. to the company in terms of regulations 13(4) and 13(5) of SEBI (Prohibition of Insider Trading) Regulations, 1992 (hereinafter referred to as **"SEBI (PIT)"**)

b. to the company and stock exchanges in terms of regulation 7(1) read with 7(2) of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (hereinafter referred to as **"SAST"**)
c. to the stock exchange/s in terms of regulation 3(3) of SAST, 4 working days in advance of the date of the proposed acquisition as the acquisition was an inter-se transfer of shares amongst relatives.

3. It was alleged that the Noticee had violated the provisions of the said regulations and therefore, liable for monetary penalty under section 15A(b) of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as '**SEBI Act**').

APPOINTMENT OF ADJUDICATING OFFICER

4. Mr. Piyoosh Gupta was appointed as Adjudicating Officer, vide order dated August 3, 2007 under section 15 I of the SEBI Act read with rule 3 of SEBI (Procedure for Holding Inquiry and Imposing Penalty by Adjudicating Officer) Rules, 1995 (hereinafter referred to as the **'Rules'**) to inquire into and adjudge under section 15A(b) of the SEBI Act the alleged violation of regulation regulations 13(4) read with 13(5) of SEBI (PIT) and regulations 3(3) and 7(1) read with 7(2) of SAST.

5. Consequent upon the transfer of Mr. Piyoosh Gupta, the undersigned was appointed as the Adjudicating Officer vide order dated November 19, 2007

SHOW CAUSE NOTICE, REPLY AND PERSONAL HEARING

6. Show Cause Notice (hereinafter referred to as "**SCN**") dated January 4, 2008 was issued to the Noticee under rule 4 of the Rules to show cause as to why an inquiry should not be initiated against him and penalty be not imposed under section 15A(b) of SEBI Act for the alleged violation of regulations 13(4) read with 13(5) of SEBI (PIT) and regulations 3(3) and 7(1) read with 7(2) of SAST.

7. The Noticee replied vide letter dated February 9, 2008. The submissions of the Noticee, *inter alia*, are as under:

- It had already been submitted in our correspondence to the Bombay Stock Exchange Limited and Securities and Exchange Board of India

that I had informed the company on July 5, 2006 as per regulation 13(4) and 13(5) of SEBI (PIT) and regulations 7(1) and 7(2) of SAST regarding acquisition of 11,12,000 Equity Share by me from my son K Srinivas.

- It is submitted that the transfer had taken place within the family to facilitate certain family issues since the relationship between the transferor and the transferee is that of a father and son as rightly noted in your notice referred to above. Further, it may kindly be noted that no single share out of the 11,12,000 shares has been sold till date.

8. In the interest of natural justice and in terms of rule 4(3) of the Rules, the Noticee was granted an opportunity of personal hearing on April 29, 2008 vide notice dated April 15, 2008. Mr. S S Marthi appeared on behalf of the Noticee, and submitted, inter alia, as under:

- It was only a transfer and not a purchase. The transfer was made by Mr. K Srinivas to his father, the Noticee. There was no consideration involved in this transaction. The transaction took place as a part of family arrangement. With this transaction, the total shareholding of the family has not undergone any change. These shares are still with the Noticee and have not been traded in the market.

- The Noticee has not sought any exemption from the applicability of the provisions of SAST.

- As the Noticee was out of station, the disclosure under SEBI (PIT) which ought to have been made on July 4, 2006 was made on July 5, 2006.

CONSIDERATION OF ISSUES AND FINDINGS

9. I have carefully perused the written and oral submissions of the Noticee and the documents available on record The issues that arise for consideration in the present case are :

(i) Whether the Noticee has violated regulation 13(4) and 13(5) of SEBI (PIT)?

(ii) Whether the Noticee has violated regulation 3(3) of SAST?

(iii) Whether the Noticee has violated regulation 7(1) read with 7(2) of SAST?

(iv) Does the non-compliance, if any, on the part of the Noticee attract monetary penalty under section 15A(b) of SEBI Act?

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

10. Before moving forward, it is pertinent to refer to the provisions of regulations 13(4) and 13 (5) of SEBI (PIT) and 3(3) and 7 (1) and 7 (2) of SAST, 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.*
>
> *3(3) In respect of acquisitions under clauses (e), (h) and (i) of sub-regulation (1), the stock exchanges where the shares of the company are listed shall, for information of the public, be notified of the details of the proposed transactions at least 4 working days in advance of the date of the proposed acquisition, in case of acquisition exceeding 5 per cent of the voting share capital of the 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 then 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 the shares of the target company are listed.

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.

11. The Noticee is the Promoter cum Chairman and Managing Director of TBL. In terms of regulations 13(4) and 13(5) of SEBI (PIT), the Noticee is required to disclose to the company within 4 working days of the acquisition or sale of shares or voting rights if there has been change in such holdings from the last disclosure and the change exceeds Rs.5 lakhs in value or 25,000 shares or 1% of total shareholding or voting rights, whichever is lower.

12. From the documents available on record, it is observed that the shareholding of the Noticee as at the end of quarter ended March 2006 was 22.84%. There is no dispute on the fact that the Noticee had acquired 11,12,000 shares, which represented 7.4% of the total shareholding of the company, from his son Mr. K Srinivas on June 28, 2006. With the result, the change in the shareholding of the Noticee exceeded 25,000 shares and 1% of total shareholding or voting rights of TBL. Therefore, in terms of regulation 13(4) and 13(5) of SEBI (PIT), the Noticee ought to have disclosed the change in shareholding to TBL within 4 working days, i.e. on or before July 4, 2006. However, the Noticee has admitted to have made the disclosure to the company on July 5, 2006, i.e. with a delay of one day. Hence, the Noticee cannot said to have complied with the requirements of the provisions of 13(4) and 13(5) of SEBI (PIT). Therefore, the violation of the said provisions stands established.

13. As regards the alleged violation of regulation 3(3) of SAST, I would like to refer to the observations of the Hon'ble Securities Appellate Tribunal (hereinafter referred to as **"SAT"**) in the matter of *B.B. Singal V/s. SEBI* – Appeal No. 131 of 2004 – Order dated January 27, 2005. In the cited case, SAT has agreed with the contention of the Appellants in the case.

The contention of the Appellant and the SAT's decision thereon are as under:-

> "*It is the contention of the appellants that Regulation 3 comes into play only if a violation of the substantive clauses 10, 11 or 12 is first established because the very first sentence of Regulation 3 reads "nothing contained in Regulations 10, 11 and 12 of these Regulations shall apply to ……."*. .
>
> ……..
>
> *We are therefore in agreement with the appellants that before imposition of any penalty under Regulation 3 a prima facie case has to be established for violation of Regulation 10, 11, and 12. Unfortunately, however, the impugned order does not even remotely allege any violation of Regulation 10 or 11 or 12 which would have necessitated a public announcement by the acquirers. Thus, if there is no requirement of a public announcement, Regulation 3 is not at all attracted and there is no question of imposition of any penalty."*

14. In the light of the above, I am of the view that regulation 3 will come into play only if any of the substantive clauses, i.e. regulations 10, 11 or 12 of the SAST is/are first attracted. Further, on a careful reading of regulation 3(3) of SAST, I find that acquisitions falling under regulations 3(1)(e), (h) and (i) of SAST needs to be notified by the acquirer to the stock exchanges in case the acquisition exceeds 5% of the voting capital of the company. Though, in the instant case, the acquisition exceeded 5%, there is nothing on record to show that the Noticee had sought exemption from the applicability of the provisions of regulation 11(1) under regulation 3 of SAST. Since the Noticee had not submitted himself under regulation 3 and sought exemption from the applicability of regulation 11(1), I am of the view that regulation 3(3) of SAST was not attracted and therefore, I hold that there was no requirement to disclose the said acquisition under regulation 3(3) of SAST. When regulation 3(3) does not apply, the question of its violation cannot arise.

15. In terms of regulation 7(1) of SAST, 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 5% or 10% or 14% or 54% or 74% is required to disclose at every stage the aggregate of his shareholding. The disclosure is required to be made within two days of the acquisition of shares or voting rights. A plain reading of the provisions of regulation 7(1)

indicates that to prevent a league between two or more persons in the matter of acquisition of substantial shares in a company, efforts have been made to identify those persons, who may make such league, in the said definition. I am of the view that the provisions of the regulation 7(1) of SAST would be attracted by a person or a group of persons acting in concert, when overall post–acquisition holding crosses 5% or 10% or 14% or 54% or 74%.

16. The SAST made under SEBI Act was framed basically taking into consideration the recommendations of the committee chaired by Justice (retd.) P N Bhagwati. It is necessary to go behind the regulatory requirements to discover their *raison de etre* and the fundamental principles on which these regulations are predicated. It will be appropriate to refer to the recommendation of the committee with regard to disclosure requirements as stated in para 15 of Justice P.N. Bhagwati Committee Report on Takeovers dated May 7, 2002. After deliberations the Committee recommended that –

- *Disclosure should be made at every stage when the acquirer crosses the limit of 5%, 10% and 14%;*

- *for acquirers holding 15% and above , purchases and sales for every 2% level should be disclosed;*

- *the reporting of acquisitions/ sales should be made to the stock exchanges and to the target company within two days.*

17. Based on the aforesaid recommendations, regulation 7(1A) was inserted in the statute book with effect from October 24, 2001 and subsequently modified with effect September 9, 2002. Accordingly, regulation 7(1A) as existed in 2006 reads as under:

> *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.*

18. On perusal of the documents available on record, it is observed that the individual shareholding of the Noticee was 22.84% and the collective shareholding of the promoter group was 40.6% as at the quarter ended March 2006. Since the Noticee, individually as well as collectively, held more than 15% but less than 55% as of June 27, 2006, i.e. one day prior to the date of acquisition of 11,12,000 shares representing 7.4% of the voting capital of TBL, I am of the view that the said acquisition made by the Noticee attracted the provisions of regulation 7(1A) and not regulation 7(1) as alleged. When regulation 7(1) does not apply, the question of its violation cannot arise.

19. In the light of the aforesaid findings, I conclude that out of the three allegations made against the Noticee, only violation of regulation 13(4) read with regulation 13(5) of SEBI (PIT) is established, i.e. because of delay in disclosure by one day.

20. There is nothing on record to show that the aforesaid one day delay in making the disclosure resulted in any disproportionate gain or unfair advantage to the Noticee or any loss to an investor or group of investors. There is also nothing on record to show that the Noticee had a past record of default.

ORDER

21. After taking into consideration all the facts and circumstances of the case and material available on record and on exercise of the judicial discretion, I am of the view that it is not a fit case to impose any monetary penalty on the Noticee and the matter is, accordingly, disposed of.

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

Date: **June 24, 2008** **V.S.SUNDARESAN**
Place: **Mumbai** **ADJUDICATING OFFICER**