M/S. Winsome Yarns Ltd vs Sebi on 19 July, 2022

Author: Tarun Agarwala

Bench: Tarun Agarwala

BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Date of Hearing : 1.6.2022
Date of Decision : 19.7.2022

Appeal No.716 of 2021

M/s. Winsome Yarns Ltd.
SCO 191/192, Sector 34-A,
Chandigarh-160022. ...Appellant

Versus

Securities and Exchange Board of India
SEBI Bhavan, Plot No.C-4A,
Bandra Kurla Complex, Bandra (E),
Mumbai 400 051. ...Respondent

Mr. Sajeve Bhushan Deora, Advocate with Ms. Rasika Ghate, Advocate i/b. Triad Law Chambers and Mr. Manish Bagrodia, MD for the Appellants.

Mr. Sumit Rai, Advocate with Ms. Nidhi Singh, Ms. Deepti Mohan, Ms. Binjal Samani, Ms. Aditi Palnitkar and Ms. Moksha Kothari, Advocates i/b. Vidhii Partners for the Respondent.

With
Appeal No.717 of 2021

Mr. Manish Bagrodia
House No.351,
Sector 9-D,
Chandigarh - 160009. ...Appellant

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Versus

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CORAM: Justice Tarun Agarwala, Presiding Officer
Ms. Meera Swarup, Technical Member

Per: Justice Tarun Agarwala, Presiding Officer

1.

Two appeals have been filed against the order dated 28th May, 2021 passed by the Adjudicating Officer ('AO' for short) wherein a penalty of Rs.11 crores has been imposed on noticee no.1, Winsome Yarns Ltd. i.e. the Company under Section 15HA of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as 'SEBI Act') and Section 23E of the Securities Contracts (Regulation) Act, 1956 (hereinafter referred to as 'SCRA Act') and a penalty of Rs.1 crore has been imposed upon noticee no.2, Mr. Manish Bagrodia under Section 15HA of the SEBI Act.

2. The facts leading to the filing of the present appeal is, that the Board of Directors of the Company known as Winsome Yarns Ltd. passed a resolution on 3rd September, 2010 for opening a bank account with European American Investment Bank AG (hereinafter referred to as 'EURAM Bank') for depositing the GDR proceeds. By the said resolution, the Managing Director was also authorised to sign and execute an agreement as may be required by the bank and take such steps from time to time on behalf of the Company. The resolution further resolved to use the funds so deposited in the aforesaid bank account as security in connection with loan, if any, as well as to enter into any escrow agreement or similar arrangements if and when so required.

3. The resolution approved by the Board of Directors resolved that a bank account would be opened with European American Investment Bank AG (hereinafter referred to as 'EURAM Bank') for the purpose of receiving the subscription money in respect of GDR issue. Further, Mr. Manish Bagrodia, Managing Director of the Company was authorised to sign and execute an agreement as may be required by the Bank and take such steps from time to time on behalf of the Company. The resolution further resolved to use the funds deposited in the aforesaid Bank account as security in connection with the loan, if any as well as to enter into any escrow account or similar arrangement if and when so required.

4. Based on the aforesaid resolution, the Company issued 1.99 million GDRs for USD 13.24 million dated 29th March, 2011. The aforesaid GDR was subscribed by one entity, namely, Vintage FZE (hereinafter referred to as 'Vintage') and a corporate announcement was made by the Company that the entire issue was subscribed.

5. Securities and Exchange Board of India (hereinafter referred to as 'SEBI') conducted an investigation pertaining to the issue of GDR by the Company. Based on the investigation, a show cause notice dated 11th September, 2019 was issued to the Company and its Directors to show cause as to why suitable directions under Section 11 and 11B should not be issued for violation of Section 12A(a), (b), (c) of the SEBI Act read with Regulation 3(a), (b), (c), (d) and 4(1), 4(2)(f), (k), (r) of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (hereinafter referred to as 'PFUTP Regulations'), Section 21 of the Securities Contracts (Regulations) Act, 1956 (hereinafter referred to as the 'SCR Act') read with Clauses 32, 36(7) and 50 of the Listing Agreement and Section 23E of the SCR Act.

6. The show cause notice alleged that pursuant to the resolution dated 3rd September, 2010 not only a bank account was opened with EURAM Bank but the Managing Director executed a pledge agreement dated 22nd March, 2011 on behalf of the Company based on which a loan agreement dated 22nd March, 2011 was executed between Vintage and EURAM Bank in which the proceeds of the GDR was to be kept as security with EURAM Bank. The show cause notice further alleged that the pledge agreement and the loan agreement was not disclosed to the stock exchange and, consequently, the investors and shareholders were kept in the dark. The show cause notice further alleged that based on the pledge agreement and the loan agreement EURAM Bank advanced USD 13.24 million to Vintage which amount was utilised by Vintage to subscribe to the entire issue. The GDR proceeds were pledged as security till such time the loan was repaid by Vintage. It was also alleged that the fact that Vintage was the sole subscriber was not intimated to the stock exchange and to the Indian investors and, accordingly, the Company and its Directors were charged with violation of Section 12A of the SEBI Act and Regulations 3 and 4 of the PFUTP Regulations.

7. The AO after considering the evidence on record found that the entire scheme of using the GDR proceeds to fund a subscriber to the GDR issue was a fraudulent scheme and violative of Section 12A of the SEBI Act and Regulations 3 and 4 of the PFUTP Regulations. The AO found that the GDR was subscribed by one entity, namely, Vintage and not by six entities as disclosed by the Company vide its letter dated 6th July, 2015. The AO further found that on account of the pledge created by the Company with EURAM Bank the funds were not made available at the Company's disposal and the same became available in tranches as and when the loan amount was repaid by Vintage. Further, the loan agreement was not disclosed to the stock exchange and to the Indian investors. Further, the disclosure made by the Company to the stock exchange that the GDR issue was fully subscribed was misleading as the investors were not informed that the GDR was subscribed by only one entity and, therefore, the scheme hatched by the Company and its Directors was violative of Section 12A of the SEBI Act and Regulations 3 and 4 of the PFUTP Regulations.

8. The AO found that the non-disclosure of the loan agreement and the pledge agreement was violative of Clause 36 of the Listing Agreement as well as Section 21 of the SCRA Act read with

Clause 32 and 50 of the Listing Agreement since the Company had not complied with the accounting standards and since the balance lying in the EURAM Bank was not free cash. The AO, however, found that Vintage repaid the loan amount over a period of time in instalments.

9. We have heard Mr. Sajeve Bhushan Deora, Advocate assisted by Ms. Rasika Ghate, Advocate for the appellants and Mr. Sumit Rai, Advocate assisted by Ms. Nidhi Singh, Ms. Deepti Mohan, Ms. Binjal Samani, Ms. Aditi Palnitkar and Ms. Moksha Kothari, Advocates for the Respondent.

10. The appellants contended that the entire fraudulent scheme was executed by the Lead Manager, Pan Asia Advisors Ltd. and its connected entities and that the appellants are a victim of exploitation by Vintage, Pan Asia Advisors Ltd. and other entities. The appellants denied that they have committed fraud or violated any provision of law and contended that the appellants have been subjected to the fraudulent scheme purported by Pan Asia Advisors Ltd., Vintage etc. The appellants contended that they were not in any manner connected with Vintage. Further, they had no knowledge about Vintage being the sole subscriber to the GDR issue until the receipt of the show cause notice. The appellants further denied that they had violated any clause of the Listing Agreement and contended that all information was duly disclosed to the stock exchange as and when a material event had occurred. The appellants further denied signing the pledge agreement and contended that it had never authorised EURAM Bank to create a pledge and only came to know when the show cause notice was issued. It was urged that the GDR proceeds were utilised in accordance with the objects of the GDR and there was no diversion of money nor has the appellant indulged in any wrong doing. Further, there was no complaint with regard any unlawful or disproportionate gain or any loss caused to the shareholders or to the investors. It was urged that the appellant, being a small Company, has not played any fraud upon the market and violation, if any, is confined to non-disclosure under the Listing agreement for which purpose the penalty awarded was wholly excessive, harsh and disproportionate.

11. It was urged that all approvals and compliances were met by the appellant Company pertaining to the GDR issue from BSE and NSE and filing with the Luxembourg Stock Exchange for listing of the GDR which eventually led to the approval and the issue of GDR. It was also urged that Pan Asia Advisors Ltd., were renowned Lead Managers and registered in U.K. and were known to have conducted several GDRs and based on their reputation had appointed Pan Asia Advisors Ltd. as Lead Manager who advised the Company on how to proceed with the GDR without realising that they had played a fraud upon the Company and its Directors. It was contended that post GDR issue the GDR funds were moved from the escrow account to current account with EURAM Bank. Further, BSE and NSE approved the listing of securities and Luxembourg Stock Exchange listed the GDR for trading and filings were completed with Reserve Bank of India ('RBI' for short). It was contended that the returns as prescribed by RBI was duly filed by every quarter and within the time provided for the purpose. As per the provisions of the master circular issued by RBI dated 2nd July, 2007 it was contended that the funds raised in overseas market was required to be maintained outside India and if not utilised it should be brought back to India when to be put to use. It was contended that this circular was duly followed and returns as prescribed by RBI was duly filed.

12. The appellant contended that as per the listing prospectus the GDR proceeds were required to be utilised in the following manner.

Capital expenditure for setting up a 10MT Dyeing Unit at Derabassi Strengthening of Net Working Capital Overseas Investments Other Corporate purposes

13. It was urged that the proceeds have been utilised for the purpose shown in the listing prospectus. It was urged that the GDR funds of USD 3,78,865 were utilised to pay cost of the issue. USD 9,33,004 were utilised overseas and USD 71,66,925 were received in India towards strengthening the networking of the Company. It was contended that more than 60% of the funds have come back to India and has been utilised as per the purpose specified in the listing prospectus. It was also urged that the GDR funds amounting to USD 47,62,125 which was to be used for setting up Yarn Dying Plant abroad could not be utilised on account of recession as a result of which the amount had remained invested in the money market instrument with Aries Capital Fund Ltd., which is a fund in Mauritius and regulated by Financial Services Commission of Mauritius. It was urged that the said amount has increased to USD 48,19,990 as on 31st December, 2019 and 49,73,276.84 as on 31st December, 2020

14. It was also urged that the appellants had engaged a professional for managing the issue and other connected matters post the issue. The appellant had appointed the Bank of New York and Mellon which acted as a Depository Bank and Development Bank of Singapore acted as a custodian of GDR. Further, Sharma & Co. (London) was appointed as a Legal Counsel who rendered legal opinion that all acts, deeds and things done were in compliance with the applicable law and that Lex Favios, New Delhi were appointed as the Indian Legal Advocate who rendered legal opinion that all acts, deeds and things of the parties were in compliance with applicable laws in India. It was, thus, contended that due diligence was complied at all levels and there was no intent to get involved in any fraudulent scheme.

15. On the other hand, the respondent supported the impugned order and contended that the modus operandi is the same as has been dealt with by this Tribunal in a large number of matters relating to the GDR issue wherein this Tribunal has held that the non- disclosure of the loan agreement and the pledge agreement was totally fraudulent and violative of the Listing Agreement.

16. Having heard the learned counsel for the parties, in our opinion, the contentions raised by the appellant cannot be accepted. The signature of the Managing Director/Director on the pledge agreement has not been disputed before us and it cannot be believed that such signatures on such important documents were signed without their knowledge or in ignorance or in good faith at the instance of the Lead Manager. Further, when they came to know of the fraud, no steps were taken to lodge a complaint or an FIR. Not only this, we find that based on the pledge agreement, the GDR proceeds were blocked for a certain period of time and it was not possible for the Company and its Directors to contend that they were not aware that the GDR proceeds had been frozen on account of the pledge agreement. Thus, in view of the aforesaid we are of the firm view that the appellants were aware of the execution of the pledge agreement and had signed with open eyes and had knowledge. The appellants consequently cannot deny the existence of the loan agreement executed between

Vintage and EURAM Bank.

17. The appellants also misled SEBI into believing that there were six subscribers to the issue. Investigation found that there was only one subscriber. Explanation given by the Company and its Directors that the Lead Manager had supplied the information which were forwarded to SEBI in good faith cannot be believed. At the end of the day, the responsibility lies with the Company to forward such information which are true and the blame cannot be passed to another entity.

18. Since we have already held that the appellants were aware of the pledge agreement, non-disclosure of the pledge agreement invited penalty. Further, the corporate announcement did not disclose the fact that the subsisting pledge agreement facilitated one subscriber to subscribe to the GDR issue. The corporate announcement was misleading and presented a distorted version to the investors and created a false version inducing the investors to deal in securities.

19. There is no doubt that the proceeds of the GDR issue was eventually received by the Company. More than 60% i.e. USD 71,66,925 has been received in India and has been utilised as per the Listing prospectus. A sum of USD 47,62,125 which was to be utilised for setting up a subsidiary plant abroad which has swelled up to USD 49,73,276.84 as on 31st December, 2020 remains invested in money market instruments with Aries Capital Fund Limited. These facts have not been disputed by the respondent. Thus, there has been no diversion of money and there is no wrongful dealing in securities other than the fact that USD 6.05 million was deducted by EURAM Bank for a default committed by Vintage. The AO has himself given a finding that no disproportionate gain is attributed to the appellants. No finding has been given by the AO that any loss was caused to the shareholders or investors.

20. We are accordingly of the opinion that in view of the fact that the appellant is a small listed Company the directions issued by the WTM and the penalty imposed by the AO is excessive and arbitrary as well as discriminatory.

21. In Excel Corp. (supra) the Supreme Court held:

> "92. Even the doctrine of „proportionality would suggest that the court should lean in favour of „relevant turnover . No doubt the objective contained in the Act, viz., to discourage and stop anti-competitive practices has to be achieved and those who are perpetrators of such practices need to be indicted and suitably punished. It is for this reason that the Act contains penal provisions for penalising such offenders. At the same time, the penalty cannot be disproportionate and it should not lead to shocking results. That is the implication of the doctrine of proportionality which is based on equity and rationality. It is, in fact, a constitutionally protected right which can be traced to Article 14 as well as Article 21 of the Constitution. The doctrine of proportionality is aimed at bringing out „proportional result or proportionality stricto sensu . It is a result oriented test as it examines the result of the law in fact the proportionality achieves balancing between two competing interests: harm caused to the society by the infringer which gives justification for penalising the infringer on

> the one hand and the right of the infringer in not suffering the punishment which may be disproportionate to the seriousness of the Act."

22. Similar view was expressed by the Delhi High court in Rajkumar Dyeing and Printing Works Pvt. Ltd. In Rajendra Yadav, the Supreme Court held that the doctrine of equality applies to all those who are found guilty. The Supreme Court held:

> "9. The doctrine of equality applies to all who are equally placed; even among persons who are found guilty. The persons who have been found guilty can also claim equality of treatment, if they can establish discrimination while imposing punishment when all of them are involved in the same incident. Parity among co-delinquents has also to be maintained when punishment is being imposed. Punishment should not be disproportionate while comparing the involvement of co-delinquents who are parties to the same transaction or incident. The disciplinary authority cannot impose punishment which is disproportionate, i.e., lesser punishment for serious offences and stringent punishment for lesser offences."

23. Undoubtedly, the doctrine of proportionality is now well established in our jurisprudence and is a recognised facet of Article 14 of the Constitution of India. In Andhra Pradesh Dairy Development Corporation Federation vs. B. Narasimha Reddy and Others (2011) 9 SCC 286, the Supreme Court held:

> "29. It is a settled legal proposition that Article 14 of the Constitution strikes at arbitrariness because an action that is arbitrary, must necessarily involve negation of equality. This doctrine of arbitrariness is not restricted only to executive actions, but also applies to legislature. Thus, a party has to satisfy that the action was reasonable, not done in unreasonable manner or capriciously or at pleasure without adequate determining principle, rational, and has been done according to reason or judgment, and certainly does not depend on the will alone. However, the action of legislature, violative of Article 14 of the Constitution, should ordinarily be manifestly arbitrary. There must be a case of substantive unreasonableness in the statute itself for declaring the act ultra vires of Article 14 of the Constitution. (Vide: Ajay Hasia etc. v. Khalid Mujib Sehravardi, Reliance Airport Developers (P) Ltd. v. Airports Authority of India, Bidhannagar (Salt Lake) Welfare Assn. v. Central Valuation Board, Grand Kakatiya Sheraton Hotel and Towers Employees and Workers Union v. Srinivasa Resorts Limited, and State of T.N. v. K. Shyam Sunder.)"

24. In matters relating to punitive measures the emphasis has shifted from the wednesbury principle of unreasonable to one of proportionality. A disproportionate punitive measure which does not commensurate with the offence would be violative of Article 14 of the Constitution of India. We are of the opinion that in the rapid growth of administrative law it has become the need and necessity to control possible abuse of discriminatory power by administrative authorities. In this regard, certain principles have been evolved by Courts, namely, that if an action is taken by an authority which is contrary to law or which is improper or where the action taken is unreasonable

then the Court of law is duty bound to interfere with such action and one such mode of exercising power is to exercise the doctrine of proportionality. Where the punitive measure is harsh or disproportionate to the offence which shocks the conscience it is within the discretion of the Court to exercise the doctrine of proportionality and reduce the quantum of punishment to ensure that some rationality is brought to make unequals equal.

25. A penalty has also been imposed for violation of Section 23E of the SCRA Act for non-disclosure under the Listing Agreement. The imposition of penalty under Section 23E is wholly erroneous in as much as Section 23E is not applicable.

26. In Suzlon Energy Ltd. v. SEBI, appeal no.201 of 2018 decided on 3rd May, 2021, this Tribunal held:

> "17. The AO held that since Clause 36 of the Listing Agreement was violated, in addition to the penalty imposed under Section 23A(a), the provisions of Section 23E of the SCRA is also invoked. In our view, the imposition of penalty under Section 23E is patently erroneous. The AO has committed a manifest error in invoking Section 23E of the SCRA.
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> 18. Section 23E has nothing to do with the violation of the provisions of the Listing Agreement especially Clause 36. Section 23E provides that where a Company fails to comply with the listing conditions or delisting conditions or grounds or commits a breach thereof then penalty would be a minimum of Rs. 5 lakh upto maximum of Rs. 25 crore. The words "fails to comply with the listing conditions" cannot mean failure to comply with the conditions in the Listing Agreement. One of the requirements in the Listing Agreement which is required to be complied with is Clause 36 whereas Section 23E refers to the conditions which are imposed upon a Company when it is applying for its shares to be listed on the stock exchange platform. Section 23E has to be read along with Rule 19 of the Securities Contracts (Regulation) Rules, 1957 („SCRR for short). Rule 19 of the SCRR provides certain requirements with respect to a listing of securities on a recognized stock exchange. Rule 19A provides that a Company has to continuously maintain listing requirements. Rule 21 provides conditions for delisting of securities. Failure to comply with the listing conditions which are stated in Rule 19 would entail a penalty as provided under Section 23E. Thus, in our view violation of Clause 36 of the Listing Agreement will attract Section 23A(a) of the SCRA and will not attract Section 23E. The AO has made an error.
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> 19. In view of the aforesaid, the penalty of Rs. 1 crore under Section 23E is patently erroneous and cannot be imposed and the order to that extent cannot be sustained."

27. In this regard, the appellants have produced various orders passed by SEBI against various companies and its Directors wherein different penalties have been imposed for similar/identical offence. In the instant case, the AO has penalised the appellant Company of Rs.11,00,00,000/- and the Managing Director Rs.1,00,00,000/-. In similar matters lesser penalty has been awarded. For

facility, a comparative table is given hereunder:

Penalty Orders	Sr.	Name of the issuer	Date of GDR Issue	Subscriber	Combined size	Date of Penalty	No. of the company	GDR Order	(million $)
1.	ABL	June 2008	6.68	Clifford Capital Partners	Rs.50,00,000/- (Rupees Fifty Lakhs)	23rd April, 2018	Ltd.		
2.	Syncom Healthcare Ltd.	September 2010	20.74	Vintage	Rs.25,00,000/- (Rupees Twenty Five Lakhs)	30th August, 2019			
3.	Visu International Ltd.	April 2006	9.66	Seazun	Rs.1,25,00,000/- (Rupees 1 Crore Twenty-Five Lakhs)	18th March, 2021			
4.	GV Films Ltd.	April 2007	40	Whiteview	Rs.25,00,000/- (Rupees Twenty-Five Lakhs)	29th January, 2020			
5.	Aksh Opti- Fibre Ltd.	Sept 2010	25	Vintage	Rs.10,15,00,000/- (Rupees Ten Crore Fifteen Lakhs)	28th February, 2020			
6.	Rana Sugars Ltd.	May, 2006	18.00		Rs.10,00,000 (Rupees Ten Lakhs)	28th February, 2018			
7.	Sybly Industries Ltd.	June 9, 2008	6.99	Vintage	Rs.10,30,00,000/- (Rupees Ten Crore Thirty Lakhs)	March, 2019			
8.	Winsome Yarns Ltd.	March 29, 2011	13.24	Vintage	Rs.11,00,00,000 (Rupees Eleven Crores)	28th March, 2021			

28. A perusal of the aforesaid table indicates that G.V. Films Ltd. had raised 40 million USD and the Company was only awarded a penalty of Rs.25,00,000/-. Another Company Syncom Healthcare Ltd., raised 20.74 million USD and was awarded a penalty of Rs.25 lakhs whereas in the case of the appellant Company who raised 6.99 million USD has been awarded Rs.10,30,00,000/-. In Sybly Industries Ltd. v. SEBI, appeal no.381 of 219 and other connected appeals decided on 14th July, 2022 penalties ranging from Rs.10 lakhs to Rs.10.30 crores were imposed which were reduced to Rs.25 lakhs on the Company and Rs.10 lakhs on the Managing Director. Thus, in our opinion, the penalty imposed is excessive and disproportionate to the violation and is also discriminatory.

29. We find that such excessive penalty imposed upon the Company does not make any sense. In the instant case, there are public shareholders and workers. The Company is a running concern. Penalising the Company with such heavy penalty is in fact penalising the shareholders which is not justifiable especially for a running company. Further, the money raised through GDRs has been received by the Company and has not been misappropriated. The same has been utilitised for the purpose for which the GDR was issued which fact has not been disputed. Thus, it is not a case of

defalcation of the funds.

30. Consequently, while affirming the order of the AO for the violations committed by the Company we reduce the penalty against the Company to Rs.25 lakhs and the penalty against the Managing Director to Rs.10 lakhs. The appeals are partly allowed.

31. This order will be digitally signed by the Private Secretary on behalf of the bench and all concerned parties are directed to act on the digitally signed copy of this order. Certified copy of this order is also available from the Registry on payment of usual charges.

Justice Tarun Agarwala Presiding Officer Ms. Meera Swarup Technical Member RAJALA Digitally by signed KSHMI NAIR RAJALAKSHMI H 19.7.2022 Date: 2022.07.21 H NAIR 14:12:28 +05'30' RHN