BEFORE THE SECURITIES APPELLATE TRIBUNAL MUMBAI

Appeal No. 186 of 2011

Date of decision: 2.11.2011

Aditya Birla Finance Ltd.
Indian Rayon Compound,
Veraval,
Gujarat – 362 266. …Appellant

Versus

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

2. Mentor Capital Limited
   (Previously known as Pacific Corporate Services Limited)
   713, Raheja Centre,
   Nariman Point, Mumbai 400 021. … Respondents

Mr. R. S. Loona, Advocate with Mr. Abhishek Borgikar, Advocate for the Appellant.

Mr. Shiraz Rustomjee, Senior Advocate with Ms. Daya Gupta, Ms. Harshada Nagare, Advocates for Respondent no. 1.

Mr. P. N. Modi, Advocate with Ms. Manik Joshi, Ms. Amrita Nandgaonkar, Advocates for Respondent no. 2.

CORAM : Justice N. K. Sodhi, Presiding Officer
P. K. Malhotra, Member
S. S. N. Moorthy, Member

Per : Justice N. K. Sodhi, Presiding Officer (Oral)

Aditya Birla Finance Limited, the appellant herein is a non-banking finance company registered with the Reserve Bank of India and engaged in the business of providing credit facilities to its clients. It shall be referred to hereinafter as the lender. It provided a loan facility to Mentor Capital Limited, the second respondent which was formerly known as Pacific Corporate Services Limited. This respondent shall be referred to hereinafter as the borrower. The borrower entered into a loan agreement with the lender on June 2, 2010 and several other security related documents had been executed between them. As per

this agreement the borrower could purchase and sell any securities which were approved by the lender only through a broker approved by the latter. It was also stipulated between the lender and the borrower that the latter shall maintain a designated demat account with an approved depository participant. It is common ground between the parties that the approved broker and the depository participant in the present case was Aditya Birla Money Limited as it was a registered stockbroker and a depository participant. It is the case of the lender that the approved broker and the depository participant is its group company which fact is not disputed by the borrower. As per the loan agreement, the borrower had opened an approved bank account with HDFC Bank and also an approved demat account with Aditya Birla Money Limited. In terms of the loan agreement, the borrower had also executed irrevocable powers of attorney in favour of the lender by virtue of which the latter alone could operate the approved bank account and the demat account. It was also the requirement of the loan agreement that the securities purchased by the borrower shall be pledged with the lender and in this regard a deed of pledge had also been executed between the parties though the procedure required for creating a pledge as required by Section 12 of the Depositories Act, 1996 read with Regulation 58 of the Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996 had not been followed. The lender contends that the creation of a pledge as required by the aforesaid provisions of law was not a condition precedent for the disbursement of the loan under the loan agreement. Be that as it may, we have on record that with the money lent by the lender, the borrower purchased the securities of four companies namely, Mahindra Forging Limited, Indusind Bank Limited, Hindusthan Oil Exploration Company Limited and Welspun Corp Limited. It is pertinent to mention here that the shares of Welspun Corp Limited were purchased by the borrower between November 5, 2010 and November 16, 2010.

2. On receipt of information from the office of the Assistant Commissioner of Income Tax, Nagpur, the Securities and Exchange Board of India (for short the

Board) carried out investigations in the scrip of Murli Industries Ltd. The scope of the investigations was expanded and the Board brought under its scrutiny the scrips of four other companies namely, Ackruti City Limited, Brushman India Limited, Welspun Corp. Limited and RPG Transmission Limited. During the course of the investigations, the Board prima facie found that the promoters alongwith several other entities had manipulated the scrips of these companies. In view of the prima facie findings, the Board by its order dated December 2, 2010 restrained, among others, the borrower from accessing the securities market and prohibited them from buying, selling or dealing in securities in any manner till further directions. This ex-parte order was treated as a show cause notice and the entities which had been restrained including the borrower were required to file their replies. After hearing the parties, the ex-parte ad-interim order was confirmed against the borrower and others on July 19, 2011. We are only concerned with the borrower in this appeal. Feeling aggrieved by the order of July 19, 2011, the borrower filed Appeal no. 183 of 2011 before this Tribunal challenging the findings recorded therein. Since the investigations were going on and we are informed that they are still continuing, we did not go into the merits of the issues sought to be raised before us and disposed of the appeal by directing the Board to conclude the investigations before the end of this year. The borrower made a prayer in that appeal that being an investment company it had a large portfolio of investments the value of which was close to ` 600 crores and that in view of the falling market it should be allowed to sell the stocks held by it by way of investment so as to reduce the losses. While not interfering with the merits of the impugned order, we granted this prayer subject to the condition that the amounts realized by such sales be deposited in an escrow account. The borrower also wanted to utilize the sale proceeds to meet with its outstanding liabilities including government dues. In this regard, we directed the borrower to seek the permission of the Board. The matter rested at that.

3. In the meantime, the lender by its letter dated December 6, 2010 called upon the borrower to pay the outstanding amount in the loan account. Since the

borrower failed to do that, the lender approached the Board by its letter of February 4, 2011 seeking permission to transfer the securities lying in the demat account of the borrower to its own demat account and further sought permission to sell the same to recover the loan amount. The Board by its letter dated March 28, 2011 rejected the request made by the lender upon which the latter filed Appeal no. 110 of 2011 before this Tribunal which was disposed of on September 2, 2011 on an agreement between the parties. It was agreed that the lender shall approach the Board with all the relevant records and the Board would examine the request and pass an appropriate order. The needful was done and by letter dated October 14, 2011, the request of the lender has again been turned down. It is against this communication that the present appeal has been filed.

4. We have heard the learned counsel for the parties including the learned senior counsel for the Board. Investigations in the matter are still continuing and whether the borrower had played any mischief while trading in the scrips of five companies as aforesaid including Welspun Corp Limited is yet to be ascertained. It is not in dispute that with the funds received from the lender, the borrower had traded in the scrips of four companies, three of which are not under the scanner of the Board. It is common ground between the parties that the scrips of Mahindra Forging Limited, Indus Ind Bank Limited and Hindusthan Oil Exploration Company Limited are not under investigations and only the scrip of Welspun Corp Limited is being looked into by the Board. In the case of Welspun Corp Limited, the shares were purchased by the borrower between November 5, 2010 and November 16, 2010. The loan agreement was executed between the parties on June 2, 2010. The period for which the scrip of Welspun Corp Limited is being investigated is not only prior to the period when the borrower purchased the shares but also prior to the date of the loan agreement. The learned senior counsel appearing for the Board informs us that the dealings in the scrip of Welspun Corp Limited are being investigated for the period between January 2009 and March 2010. This being the position and having regard to the equities of the case and also taking note of the fact that there is not a whisper about any wrong doing on

the part of the lender, it would be reasonable and fair to allow the prayer made by it. As already noticed earlier, the prayer made by the borrower to sell the shares to reduce the losses has already been granted. In this view of the matter, we set aside the impugned order and issue the following directions:-

(i) The demat account of the borrower with the designated/approved depository participant shall be unfrozen for the limited purpose of transfer of shares to the demat account of the lender.

(ii) The lender shall be at liberty to sell the shares to the extent necessary to recover its outstanding dues. The shares, if any, that remain after recovering its dues shall be retransferred by the lender to the demat account of the borrower with J. M. Financial Services Private Limited (demat a/c no. 10017965 – DPID no. IN302927). The lender is directed to inform the Board and the borrower soon after the sales are made and shall also furnish to them copies of the contract notes. The details of the loan adjustment shall also be furnished to them.

(iii) The appellant undertakes that in the event it is called upon by the Board or by this Tribunal to bring back the money which it would have realized by the sale of shares, it shall do so forthwith. The undertaking is recorded. It is, however, may clear that if and when the lender is called upon to bring back the money, it shall be open to it to challenge the said direction and avail such remedies as are available in accordance with law.

5. Before concluding, we may take note of the two contentions sought to be raised by the learned senior counsel for the Board. He contends that it is irrelevant in the present case whether the shares were purchased out of the funds advanced by the lender as the Board has not taken any action against the lender. He also contends that the amount should not be allowed to be realized since a

valid pledge has not been created in accordance with Depositories Act and the Regulations framed thereunder.

6. It is not necessary to adjudicate upon the first contention. As regards the second contention, it is nobody's case that a valid pledge in terms of Section 12 of the Depositories Act read with Regulation 58 of the aforesaid regulations had been created. The learned senior counsel also sought to contend that there are discrepancies and manipulations in the loan documents that were produced before the Board and the ones annexed to the earlier appeal filed by the lender. There is no mention of any discrepancy either in the impugned order nor has the Board filed a reply in the present case raising this issue. Therefore, we have not allowed this plea to be raised now for the first time before us during the course of the arguments. We are also making it clear that nothing stated hereinabove should be taken as an expression of our view on the merits of the issues that may come up for the consideration of the Board during or after the investigations.

In the result, the appeal is allowed as above with no order as to costs.

Sd/-
Justice N. K. Sodhi
Presiding Officer

Sd/-
P. K. Malhotra
Member

Sd/-
S. S. N. Moorthy
Member

2.11.2011
Prepared & Compared by
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