

BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Order Reserved On: 16.05.2018

Date of Decision : 08.06.2018

Appeal No. 317 of 2017

KII Limited
CIM CORPORATE SERVICES LTD.,
Les Cascades Building,
Edith Cavell Street,
Port Louis, Mauritius ...Appellant

Versus

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

Mr. Mustafa Doctor, Senior Advocate with Ms. Divya Mundra and
Mr. Asadulla Thangal, Advocate i/b AZB & Partners for the Appellant.

Mr. P. N. Modi, Senior Advocate with Mr. Nishant Upadhyay, Advocate
i/b K. Ashar & Co. for the Respondent.

CORAM: Justice J.P. Devadhar, Presiding Officer
Dr. C.K.G. Nair, Member

Per: Justice J.P. Devadhar

1. This appeal is filed to challenge the order passed by the Whole Time Member ("WTM" for short) of Securities and Exchange Board of India ("SEBI" for short) on 05.09.2017. By the said order, appellant was prohibited from accessing the securities market directly or indirectly for a period of six years, however, the period of prohibition already undergone

pursuant to the interim order dated 21.09.2011 was permitted to be reduced while computing the prohibition of six years.

2. It is not in dispute that appellant has already undergone the prohibition of six years and as such the appeal has virtually become infructuous. However, the appellant wants to pursue the appeal for the reason that the said order passed by SEBI is erroneous and that erroneous order is affecting the credibility of the appellant in the international market and therefore, it is necessary to contest the appeal on merits.

3. Facts relevant for the present appeal are as follows:-

- a) Appellant is a private company incorporated in Mauritius, holding a Category I Global Business Licence. Appellant is also a registered sub-account with SEBI under the foreign institutional investor registration of Credo Capital Plc since November 2003. Credo Capital Plc is incorporated in England and Wales.
- b) The appellant was originally established in October 2002 by a client of Credo Capital Plc for the purpose of carrying out Global Depository Receipts (“GDRs”) / ADR arbitrage transactions in the Indian market, i.e. inter alia buying of GDRs, converting them and selling the underlying shares in India at a profit.

c) Dispute in the present case relates to the fraudulent arrangement regarding subscription of GDRs issued by 6 Indian Companies during the period from 31.03.2007 to 06.11.2009 and then converting the said GDRs and selling the underlying shares in the Indian securities market. The fraudulent arrangement was in relation to the subscription of GDRs issued by the following Issuer Companies:-

- a) Asahi Infrastructure & Projects Ltd.
- b) Avon Corporation Ltd.
- c) CAT Technologies Ltd.
- d) IKF Technologies Ltd.
- e) K Sera Sera Productions Ltd.
- f) Maars Software International Ltd.

d) PAN Asia Advisors Ltd. (PAN Asia) was the Lead Manager to the GDRs issued by the aforesaid six Issuer Companies. Mr. Arun Panchariya, a Non-resident Indian (NRI) was the Promoter and Managing Director of PAN Asia and held 100% shares of PAN Asia.

e) Prior to the issuance of GDRs by the aforesaid Issuer Companies, Vintage FZE ('Vintage'), a Dubai based company which is also 100% owned and controlled

by Mr. Arun Panchariya entered into a loan agreement with European American Investment Bank AG ('Euram Bank') by which Euram Bank advanced millions of USD worth of loans to Vintage expressly for purchasing the GDRs to be issued by the six Issuer Companies.

- f) Similarly each of the said six Issuer Companies opened accounts with Euram Bank for the purpose of crediting the GDR issue proceeds in their respective accounts with Euram Bank and each of the said six Issuer Companies pledged the said accounts to Euram Bank as security for the loans given by Euram Bank to Vintage to buy the GDRs. Pledge Agreements were also executed by each of the six Issuer Companies simultaneously along with the respective loan agreement.
- g) Thus, Vintage cornered entire GDRs of all six Issuer Companies by obtaining loan from Euram Bank and the six Issuer Companies credited the GDR issue proceeds to their respective accounts with Euram Bank and pledged their accounts to Euram Bank as security for the loan taken by Vintage from Euram Bank to buy the GDRs.

- h) The GDRs so acquired by Vintage were thereafter sold/ transferred to FIIs and their sub-accounts such as India Focus Cardinal Fund ('IFCF') which was 100% controlled by Mr. Arun Panchariya and Others such as the appellant herein.
- i) IFCF and also the appellant converted the GDRs acquired by them into underlying shares which were then sold in the Indian securities market. It is not in dispute that most of the underlying shares sold by IFCF and the appellant were purchased by the counter parties who were related to Mr. Arun Panchariya.
- j) On the basis of above facts revealed during the investigation, SEBI initiated proceedings and by an order dated 20.06.2013 held that PAN Asia and Mr. Arun Panchariya being persons associated with the securities market have acted detrimental to the interests of investors by entering into prohibited arrangement with the promoters of the six Issuer Companies. Accordingly, SEBI debarred PAN Asia and Mr. Arun Panchariya from rendering services in connection with instruments that are defined as 'securities' under Section 2(h) of Securities Contracts (Regulation) Act, 1956 ("SCRA" for short) in the Indian market or in any way dealing with them

directly or indirectly for a period of 10 years and further prohibited them from accessing capital market directly or indirectly for a period of 10 years.

- k) On appeal filed by PAN Asia and Mr. Arun Panchariya, this Tribunal by a majority decision dated 30.09.2013 set aside the decision of SEBI dated 20.06.2013 on ground that SEBI had no jurisdiction over the creation and issuance of GDRs abroad.
- l) On further appeal filed by SEBI, the Apex Court by its decision reported in (2015) 14 SCC 71 set aside the majority decision of Tribunal dated 30.09.2013 by holding that SEBI had jurisdiction to pass the order dated 20.06.2013 and restored the appeal filed by PAN Asia and Mr. Arun Panchariya for fresh decision on merits.
- m) Accordingly, the appeal filed by PAN Asia and Mr. Arun Panchariya against the decision of SEBI dated 20.06.2013 was heard afresh and by a decision dated 25.10.2016 this Tribunal dismissed the appeal and upheld the decision of SEBI dated 20.06.2013.
- n) In the meantime, by an ad-interim ex-parte order dated 21.09.2011, SEBI had restrained the entities

named therein including the appellant from dealing in securities or instrument with Indian securities as underlying in any manner whatsoever until further orders. The said ad-interim ex-parte order was confirmed against the appellant by an order dated 23.01.2013.

- o) Thereafter, on completion of investigation, show cause notice was issued to various entities including the appellant and after considering the reply and the submissions made by them including the appellant, SEBI passed the impugned order on 05.09.2017 against several entities including the appellant. By the impugned order, amongst others appellant has been prohibited from accessing the capital market directly or indirectly, and dealing in securities or instruments with Indian securities as underlying, in any manner whatsoever, for a period of six years from the date of the said order. However, the period of prohibition already undergone by the appellant pursuant to the interim order dated 21.09.2011 was directed to be reduced while computing the period of prohibition imposed by the impugned order.
- p) As noted earlier, appellant has already undergone the prohibition for six years. However, the appellant

wants to contest the matter on merits, because according to the appellant the impugned order was passed erroneously and the said erroneous order continues to affect the reputation of the appellant in the international market.

4. According to SEBI, fraud in the present case is committed on the investors in India, in two stages. Firstly, Mr. Arun Panchariya, Managing Director of PAN Asia (Lead Manager) in connivance with the six Issuer Companies subscribed to their GDRs through Vintage which was wholly owned by Mr. Arun Panchariya. Thus, the investors in India were falsely made to believe that the foreign investors have shown keen interest in the scrip of the six Issuer Companies when in fact the GDRs were not subscribed by foreign investors but by Mr. Arun Panchariya through Vintage, which was wholly owned by Mr. Arun Panchariya. Secondly, the GDRs so acquired were then transferred to IFCF (an entity controlled by Mr. Arun Panchariya) and the appellant who converted the GDRs into underlying shares and sold the said shares in the Indian securities market to the counter parties who were the entities controlled by Mr. Arun Panchariya. These transactions gave an impression that the investors in India have started subscribing to the shares of Issuer Companies when in fact the shares were sold and acquired by the entities controlled by Mr. Arun Panchariya.

5. During the course of arguments counsel for SEBI fairly stated that the appellant is not involved in the first stage of the fraud committed by

Mr. Arun Panchariya. In fact, nowhere in the impugned order it is stated that the appellant was aware of the loan taken by Vintage from Euram Bank for subscribing to the GDRs of the six Issuer Companies. Similarly, it is not stated in the impugned order that the appellant was aware of the agreement between the six Issuer Companies and Euram Bank wherein the six Issuer Companies agreed to deposit the entire GDR proceeds in the accounts opened with Euram Bank and pledge that account as security for the loan taken by Vintage for subscribing to the GDRs of the six Issuer Companies. Thus, it is not the case of SEBI that the appellant was involved in the first stage of fraud planned and executed by Mr. Arun Panchariya in connivance with the six Issuer Companies.

6. However, by the impugned order it is held that the appellant is involved in the second stage fraud committed by Mr. Arun Panchariya as the appellant had acquired GDRs on behalf of Mr. Arun Panchariya and on conversion of GDRs sold the underlying shares in the Indian securities market to the entities controlled by Mr. Arun Panchariya. Question, therefore, to be considered is, whether SEBI is justified in holding that the appellant was related to Mr. Arun Panchariya on account of the appellant acquiring GDRs belonging to Mr. Arun Panchariya and after converting the GDRs selling the underlying shares to the entities connected to Mr. Arun Panchariya and thereby create an artificial liquidity in the scrip of six Issuer Companies in violation of PFUTP Regulations.

7. Appellant is held to be related to Mr. Arun Panchariya basically for the reasons recorded in para 5.1.33 of the impugned order which reads thus:-

“

- KII is a subsidiary of Credo Investments Holding Limited (“Credo”).
- Credo Investments entered into Agreements with Vintage for obtaining loans, which were in turn lent to KII. These Agreements were signed on behalf of Vintage by Shri Arun Panchariya.
- As agreed upon in the aforesaid Agreements, the loan taken by KII from Vintage through Credo Investments was used by KII to purchase GDRs of the Issuer Companies from Vintage and thereafter, these GDRs were converted into shares and sold in the Indian securities markets.
- According to the said Agreements, the market risks of these transactions were borne by Vintage. Thus, the dealings of KII in the GDRs of the Issuer Companies were under substantial influence of Vintage who used KII to convert and dump the shares obtained from the conversion of the GDRs on the Indian investors.”

8. On the basis of aforesaid facts, SEBI has inferred that the second stage fraud was committed by Mr. Arun Panchariya with the assistance of the appellant by adopting the following modus operandi:-

- a) Vintage (controlled by Mr. Arun Panchariya) gave Millions of USD as loan to Credo to pass on the same to the appellant and the appellant agreed to use such funds to buy GDRs of the Issuer Companies from Vintage through Euram Bank, thereafter convert the GDRs into shares and sell the same in Indian markets and use the sale proceeds to repeat the same process again and again. As per the loan agreement, the profits of such trading and balance remaining funds, if any, with the appellant were to be handed over to Vintage.
- b) The underlying shares sold by the appellant were purchased by counter parties who were the entities controlled by Mr. Arun Panchariya. Thus, the appellant bought the GDRs belonging to Mr. Arun Panchariya from the loan provided by Mr. Arun Panchariya and, thereafter, sold the underlying shares to the entities controlled by Mr. Arun Panchariya. Aforesaid transactions gave a false impression that the investors in India have started showing keen interest in the shares of six Issuer Companies, when in fact the shares were bought and sold by the entities controlled by Mr. Arun Panchariya, and therefore it is held that the appellant was connected/ related to Mr. Arun Panchariya.

9. Fact that the loan agreement between Vintage and Credo was signed by Mr. Arun Panchariya on behalf Vintage under which loan was given by Vintage to Credo for being given to the appellant to buy the GDRs and sell the underlying shares in the Indian market cannot be a ground to presume that the appellant was privy to the fraud sought to be committed by Mr. Arun Panchariya, because, it is neither the case of SEBI that the said loan agreements were entered into in contravention of law nor it is the case of SEBI that the transactions permitted under the loan agreement were impermissible in law. Therefore, mere fact that Vintage controlled by Mr. Arun Panchariya had given loan to the appellant through Credo for buying the GDRs and selling the underlying shares cannot be a ground to presume that the appellant was privy to the fraud sought to be committed by Mr. Arun Panchariya on the investors in India.

10. Specific case of the appellant before SEBI was that Vintage controlled by Mr. Arun Panchariya was the client of Credo/ appellant for the past several years and as per the past experience, appellant had no reason to doubt the credibility of Mr. Arun Panchariya. That plea of the appellant is not doubted by SEBI. In such a case, mere fact that the loan agreement between Vintage and Credo was signed by Mr. Arun Panchariya for being given to the appellant for trading in GDRs under the loan agreement between Credo and the appellant could not be a ground to presume that the appellant was aware that the transactions under the said loan agreements were intended by Mr. Arun Panchariya to defraud the investors in India.

11. In any event, very fact that the WTM of SEBI has discharged the show cause noticed issued to Credo by holding (see para 5.1.45 of the order) that sufficient proof has not been made available to show direct involvement of Credo in the fraud perpetrated through the GDR issue, clearly shows that the WTM of SEBI has committed an error in arriving at a contrary conclusion in case of the appellant. If Credo who had taken loan from Vintage under the loan agreement signed by Mr. Arun Panchariya for being given to the appellant was not involved in the fraud, then by the same yard stick the appellant who got loan from Credo could not be said to have involved in the fraud. Between Credo and the appellant, Credo was directly connected to Mr. Arun Panchariya, because, he had signed the loan agreement as authorized representative of Vintage. In such a case, giving the benefit of doubt to Credo but denying the benefit of doubt to the appellant who was indirectly connected with Mr. Arun Panchairya is wholly unjustified. In other words, WTM of SEBI is not justified in holding in one breath that signing of the loan agreement between Vintage and Credo by Mr. Arun Panchariya on behalf of Vintage does not show direct involvement of Credo in the fraud perpetrated through the subscription/ trading in GDRs and in another breath holding that signing of the loan agreement by Mr. Arun Panchariya on behalf of Vintage in the loan agreement between Vintage and Credo was sufficient to hold the appellant (not a party to the contract between Vintage and Credo) was privy to the fraud sought to be perpetrated by Mr. Arun Panchariya on the investors in India.

12. Fact that on conversion of GDRs the underlying shares of the six Issuer Companies sold by the appellant in the Indian Market were bought mainly by the entities controlled by Mr. Arun Panchariya could not be a ground to hold that the appellant was privy to the fraud committed by Mr. Arun Panchariya on the investors in India, because, firstly, nowhere in the impugned order it is alleged that the appellant was aware or had known any of the counter parties to the transactions executed on the Stock Exchanges. Secondly, none of trades executed on the Stock Exchanges by and between the appellant and the counter parties controlled by Mr. Arun Panchariya have been held to have been executed in violation of the securities laws. Thirdly, even in the orders passed by SEBI against the counter parties controlled by Mr. Arun Panchariya it is not held that there was an unholy nexus between the appellant and the counter parties controlled by Mr. Arun Panchariya. Therefore, mere fact that the counter parties to the trades executed by appellant were the entities controlled by Mr. Arun Panchariya could not be a ground to hold that the appellant was privy to the fraud sought to be committed by Mr. Arun Panchariya on the investors in India.

13. Fact that the appellant did not challenge the ex-parte order dated 21.09.2011 does not mean that the appellant had accepted the prima facie view of SEBI. Very fact that the appellant cooperated with SEBI at all times clearly shows that the appellant believed that as a market regulator SEBI would consider merits of the case put forth by Credo and the appellant in the proper perspective. Unfortunately, for the appellant SEBI

has taken views in case of Credo and the appellant which are mutually contradictory.

14. During the course of arguments it was contended on behalf of SEBI that transfer of funds from Vintage to Credo and from Credo to the appellant were put in place to evade the law of Mauritius. However, we refrain from commenting on the said argument because that is not the finding recorded in the impugned order and there is nothing on record to suggest that the Mauritian authorities have held that the fund movements in the instant case were in contravention of Mauritian law.

15. Similarly, fact that the appellant instead of buying GDRs on the Luxemburg Stock Exchange, bought them from Vintage through Euram Bank and fact that the accounts between the appellant and Vintage has not been settled till date cannot be a ground to presume that the appellant was privy to the fraud committed by Mr. Arun Panchariya on the investors in India, because, neither the acquisition of GDRs from Euram Bank was prohibited nor there was any obligation on part of the appellant to terminate the contract which is found to be legal.

16 Fact that the appellant on acquisition of GDRs converted them into underlying shares and sold them in the Indian market could not be a ground to hold that the appellant had dumped the shares of the six Issuer Companies, because, in law the appellant was entitled to convert the GDRs and sell the underlying shares in the Indian market.

17. It is interesting to note that in the order passed in case of M/s Mavi Investment Fund Limited (“Mavi”) on 25.09.2013, SEBI has held that acquisition of the GDRs of the six Issuer Companies and selling the underlying shares in the Indian market by Mavi to the counter parties controlled by Mr. Arun Pancharia, do not decisively establish that Mavi was privy to the fraud committed by Mr. Arun Panchariya and accordingly gave benefit of doubt to Mavi.

18. According to SEBI benefit of doubt given to Mavi cannot be extended to the appellant for the following reasons:-

- a) Mavi’s trading was neither funded by Vintage nor by Mr. Arun Panchariya, whereas appellant’s trades were admittedly funded by Vintage controlled by Mr. Arun Panchariya.
- b) Mavi had no contract with Vintage, whereas appellant had contract with Vintage via Credo.
- c) Mavi brought GDRs of only two Issuer Companies, whereas, appellant bought the GDRs of all the six Issuer Companies.
- d) Mavi bought the GDRs from the Luxemburg Stock Exchange, whereas appellant bought the GDRs Over The Counter (OTC) from Vintage through Euram Bank.

- e) Mavi and all other FIIs who traded in the GDRs of the Issuer Companies stopped trading in such GDRs by June 2009, whereas IFCF (controlled by Mr. Arun Panchariya) and the appellant started trading in the GDRs from June 2009 onwards.

19. In our opinion, decision of SEBI based on aforesaid facts that the case of Mavi is different from the case of the appellant is wholly unjustified, because, SEBI has neither demonstrated that receiving funds by the appellant from Vintage for the trades set out in the loan agreements were contrary to law nor SEBI has demonstrated that the terms of the loan agreements directly or indirectly indicate the fraudulent intention on part of Mr. Arun Panchariya in entering into the said transactions. Therefore, when funds were received under a contract which is in accordance with law, it could not be presumed that the funds were received by the appellant for committing fraud on the investors in India. Similarly fact that Mavi bought GDRs of only two Issuer Companies from Luxemburg Stock Exchange, whereas, appellant bought GDRs of all the six Issuer Companies from Vintage through Euram Bank could not be a ground to presume that the appellant was privy to the fraud sought to be committed by Mr. Arun Panchariya, because, acquisition of GDRs from Euram Bank was neither barred nor prohibited.

20. In any event, it is not in dispute that counter parties to the trades of Mavi as also the counter parties to the trades of the appellant were the entities controlled by Mr. Arun Panchariya. In such a case, having given benefit of doubt to Mavi, SEBI is not justified in denying such benefit to

the appellant and holding, that the appellant was privy to the fraud, because, counter parties to the trades of the appellants were the entities controlled by Mr. Arun Panchariya.

21. Strong reliance was placed by counsel for SEBI on the decisions of this Tribunal and the decision of the Apex Court in case of Pan Asia reported in (2015) 14 SCC 71 in support of the contention that IFCF and the appellant were connected to Mr. Arun Panchariya. At the outset it is relevant to note that the said observations were merely reiteration of the stand taken by SEBI that IFCF and the appellant were related to Mr. Arun Panchariya and not a finding recorded after considering the plea of the appellant. In fact, appellant was not a party to the appeal filed by Pan Asia before this Tribunal. Therefore, it cannot be said that in the case of Pan Asia this Tribunal had recorded a finding that both IFCF and appellant were related to Mr. Arun Panchariya.

22. It is not in dispute that IFCF was controlled by Mr. Arun Panchariya, whereas, the relationship of Vintage (controlled by Mr. Arun Panchariya) and the appellant was only a contractual relationship which is neither held to be illegal nor contrary to law. Therefore, fact that IFCF has been found to be privy to the fraud committed by Mr. Arun Panchariya on the investors in India could not be a ground to hold that the appellant was also privy to the said fraud committed by Mr. Arun Panchariya.

23. For all the aforesaid reasons, we hold that SEBI is not justified in refusing to extend the benefit of doubt given to Credo to the appellant.

Accordingly, we quash and set aside the impugned order dated 05.09.2017 qua the appellant and as in the case of Credo, appellant is directed to ensure that all their future dealings in the Indian securities market are done strictly in accordance with law.

24. Appeal is disposed of in the aforesaid terms with no order as to costs.

Sd/-
Justice J.P. Devadhar
Presiding Officer

Sd/-
Dr. C.K.G. Nair
Member

08.06.2018
Prepared & Compared By: PK