Case Law Update

CS Makarand Joshi

Ruling of Securities and Exchange Board of India ('SEBI') – Adjudicating Officer

Name of the Case: In the matter of New Delhi Television Limited ('NDTV')

Facts of the case:

1. SEBI received a complaint dt: August 26, 2017 from Quantum Securities Pvt Ltd relating to Loan Agreements signed between Mr. Prannoy Roy (Noticee no.1), Ms Radhika Roy (Noticee no.2) and RRPR Holdings Pvt Ltd (RRPR/Noticee no.3) [Noticee no.1, Noticee no.2 and Noticee no.3 hereinafter referred to as Noticees] as one party and ICICI Bank Ltd and Vishvapradhan Commercial Private Ltd ('VCPL') as other parties. SEBI then conducted investigation to ascertain whether there was any violation of provisions of SEBI Act, 1992 while entering into loan agreements with other parties by Noticees. Noticee 1 and Noticee 2 were Chairman and Managing Director of NDTV, respectively. They were also directors and the only promoters of Noticee no.3.

2. On investigation, it was found that a corporate rupee term loan facility was entered into between RRPR and ICICI Bank on October 14, 2008 ('ICICI Bank Loan Agreement'). It was observed that ICICI Bank loan Agreement had clauses that imposed certain restrictive conditions which required NDTV to take approval of ICICI Bank before undertaking any corporate restructuring. The details of ICICI Bank Loan Agreement was not disclosed to NDTV by Noticees and hence, were not made available in public domain. Further, it was found that loan agreement dated July 21, 2009 was entered into between VCPL and the Noticees ('VCPL Loan Agreement 2009'), wherein, VCPL extended a loan of Rs 350 crore to Noticee no. 3 subject to terms and conditions of agreement. Further VCPL provided additional loan of Rs 53.85 crore to Noticee no.3 by loan agreement dated January 25, 2010 ('VCPL Loan Agreement 2010'). These agreements were also not disclosed

to NDTV by the Notices and hence, were not made available in public domain. It was further noted by SEBI that major conditions pertaining to VCPL Loan Agreement 2009 and VCPL Loan Agreement 2010 ('Loan Agreements') were same viz. promoters of NDTV permitting VCPL to acquire indirectly 30% shares of NDTV, through conversion of warrants to be issued by Noticee no. 3 to VCPL, into equity shares of Noticee no. 3, not to allow any corporate action such as merger, amalgamation, buyback etc. in the scrip of NDTV without the prior written consent of VCPL etc.

3. It was further alleged by SEBI that VCPL Loan Agreement 2010 had certain restrictive clauses which imposed certain binding conditions on NDTV and which, prima facie, required prior written consent of VCPL for such matters pertaining to NDTV. This affected interest of public shareholders of NDTV and hence was considered as material and price sensitive in nature. SEBI, further, stated that VCPL Loan Agreement 2010 should have been disclosed to NDTV by Noticees, who in turn should have disclosed the same to stock exchanges. SEBI further noted that VCPL Loan agreement (2010) and its salient features were disclosed by Noticee no. 1 to NDTV with a huge delay at the board meeting of NDTV held on August 5, 2015. Hence, it was alleged that VCPL Loan Agreement (2010) was not disclosed by the Noticees to NDTV in a timely manner. It was further alleged that Noticees had concealed the information regarding three loan agreements (viz. ICICI Bank Loan Agreement, VCPL Loan Agreement (2009) and VCPL Loan Agreement (2010)) from public while Noticee no.1 and Noticee no.2 transferred/received shares of NDTV to/from Noticee no.3 in off-market during subsistence of these agreements. Due to concealment of information from public, the Noticees have committed a fraud on minority shareholders of NDTV and due to this, general public was not able to take an informed decision regarding scrip of NDTV.

4. SEBI further alleged that by concealing information regarding these three loan agreements from NDTV and minority public shareholders and at the same time dealing in scrip of NDTV, the Noticees have failed to comply with Code of Conduct specified by NDTV. Noticees also gave false affirmations regarding compliance with Code of Conduct in annual report of NDTV for Financial Year ended 2008-09 and 2009-10.

   Charges levied: Noticees have violated Section 12A(a), (b), (c), of SEBI Act read with Regulation 3(a), (b), (c), (d) and Regulation 4(1) of PFUTP Regulations. Noticee no.1 and Noticee no. 2 have allegedly failed to comply with the Code of Conduct specified by NDTV for its Board members under Clause 49(I)(D) of Listing Agreement read with Section 21 of SCRA.

Arguments made by Noticees:

1. **Violation of Code of Conduct framed pursuant to Clause 49(I)(D)(ii) of Listing Agreement:** Noticees stated that Clause 49(1)(D) of the Listing Agreement only required a listed company to formulate

a code of conduct; table it before Board of Directors; post it on website; and for senior management and the Board to affirm compliance. Further, no gain is alleged to have accrued to the Noticees arising from any purported delay in disclosure of the Loan Agreements. There is nothing in Show Cause Notice ('SCN') to show which provision of the code of conduct stands allegedly violated by the Noticees. Further investigation report concerning ICICI Bank Loan Agreement stated as follows, "no violation of SAST regulations, listing agreement and SCRA was observed"

2. **Covenants of ICICI Bank Loan Agreement and Loan Agreements are usual business practice: Noticees stated that** Covenants imposed by ICICI Bank Ltd legitimately sought to preserve the value of the collateral security i.e. shares held by the Noticees in NDTV. Covenants mentioned in the Schedule 3 of the ICICI Loan Agreement concerning *"Matters relating to NDTV or NDTV group which require prior written consent of the Lender"* are entirely obvious from the standpoint of any lender, since it would be unreasonable to permit a corporate action to dilute or denude the value of collateral security during pendency of loan. Noticees further stated that it is usual business practice to have such covenants in place when it comes to lending against security of equity or preference shares, whether in listed or unlisted companies. In the absence of evidentiary basis in the SCN, as to how ICICI Bank Loan Agreement and VCPL Loan Agreements are adversely affecting interest of shareholders of NDTV, the allegations in SCN remains entirely ambiguous and vague. Noticees further submitted that mere entering into loan agreement does not amount to contrivance or capable of being treated as a manipulative device or artifice, and the SCN fails to put any material beyond conjecture and surmise. The assertion as to interest of public shareholders of NDTV being affected through the ICICI Bank Loan Agreement and VCPL Loan Agreements remains entirely incomprehensible.

3. **Inter-se transfer of shares between promoters cannot be considered as Fraud:** Noticees stated that loan covenants that protect the rights of a lender in the event of default are not capable of being classified as 'fraud' without cogent basis. Noticees further stated that SEBI has not shown how this inter se transfer of NDTV shares between Noticees constituted fraud on minority public shareholders. Noticees further stated that in the absence of this argument, the charge of fraud does not hold good as off-market trade between two promoters who are evenly placed in respect of access of material information, cannot be considered as violative of law. Also, SEBI has not shown who victims of fraud were.

4. **Warrants were never issued by RRPR to VCPL:** Noticees contended that even though Loan Agreements contained clause regarding issue of convertible warrants but the warrants were never issued. Merely having a clause regarding issue of convertible warrants under loan agreement cannot be considered as deceptive practice.

5. **No breach of Fiduciary duty:** Noticees contended that binding requirement to discharge fiduciary duty was duly complied. Noticees further contended that there was no scope for the loan covenants executed to interfere with the rights of the shareholders of NDTV. Fiduciary duty of the Noticees as promoters remained intact at all times, and there was no scope for breach thereof merely by virtue of the obligation to secure affirmative consent of the lender around voting on corporate actions.

6. **NDTV was not a part of VCPL Loan Agreement:** Noticees stated that VCPL Loan Agreement 2009 and 2010 could not bind NDTV as NDTV was not a part of these agreements. As NDTV was not a part of these Loan Agreements there was no scope to consider loan covenants as material/price sensitive information.

Arguments made by SEBI:

1. **Violation of Code of Conduct framed pursuant to Clause 49(I)(D)(ii) of Listing Agreement:** SEBI stated that Clause 49(I)(D) requires Board of Directors of every listed company to lay down a 'code of conduct' and compliance by the Board members and senior management of the company. Further, all the Board members and senior management of the company are required to affirm their compliance with the code on annual basis. As per provisions of Code of Conduct framed by NDTV, Board Members and Senior Management of NDTV were required to make disclosure of all facts and circumstances before making any investment, accepting any position or benefits, participating in any business transaction or business arrangement or otherwise acting in a manner that creates or appears to create a conflict of interest. Further SEBI stated that Noticee no.1 and Noticee no.2 were not only Promoters but were also Chairman and Managing Director of NDTV, respectively. They entered into ICICI Bank Loan Agreement, VCPL Loan Agreement 2009 and VCPL Loan Agreement 2010 along with Noticee no.3 which was material in nature and in conflict with interest of NDTV and its shareholders. By entering into such transaction Noticees have brought their personal interest as a shareholder in conflict with their fiduciary duty towards the interest of shareholders of NDTV. Thus, SEBI held that as per Code of Conduct of NDTV, full facts and circumstances pertaining to these loan agreements were required to be disclosed to NDTV by Noticee no.1 and Noticee no.2. Therefore, SEBI held that affirmation as required in terms of Clause 49(I)(D)(ii) of Listing Agreement as given by Noticee no. 1 and Noticee no.2 to NDTV is incorrect and so the contentions of Noticee no. 1 and Noticee no.2 are not tenable.

2. **Covenants of ICICI Loan Agreement and Loan Agreements are usual business practice:** SEBI stated that Loan Agreements had Clause which stated that the Noticees can enjoy interest free loan for a period of 10 years in case they comply with other terms and conditions most of which pertained to NDTV and acquisition of 30% stake in NDTV through the binding conditions upon Noticee no.3. Further in terms of these Loan Agreements, Noticee no.1

and Noticee no.2 were mandated to sell 22.44% of their shareholding in NDTV to Noticee no.3 so that VCPL eventually holds control over 30% of shares of NDTV by virtue of ownership of the entire share capital of Noticee no.3. In effect Loan Agreements mandated the Noticee no.1 and Noticee no. 2 to place substantial shareholding in NDTV at the disposal of VCPL as a consideration of loan amount received (i.e. Rs 403.85 crore). As per VCPL Loan Agreement 2009, Noticee no.3 was required to issue warrants to VCPL, convertible into equity shares aggregating to 99.99% of the fully diluted equity share capital of Noticee no.3 immediately upon execution of agreement. Clause 6.1 read with Schedule I of VCPL Loan Agreement 2009 provided sole discretion to VCPL to convert the warrants entitling it to have 99.99% of equity share capital of Noticee no.3. This right of conversion of warrants enabled VCPL to indirectly acquire 30% of equity shares of NDTV and same was not dependent on the repayment of loan undertaken by Noticees. SEBI further stated that an outright transfer of 30% stake and voting rights in NDTV by the Noticees to VCPL was camouflaged in form of a loan transaction which did not possess the basic attributes and characteristics of a standard secured loan transaction and were not as per industry standards. Thus, it can be inferred that the VCPL loan agreement (2009) and (2010) are sham loan transactions executed by Noticees with a motive to sell their substantial stake in NDTV to VCPL.

3. **Inter-se transfer of shares between promoters cannot be considered as Fraud:** SEBI stated that in order to comply with Loan Agreements Noticee no. 1 and Noticee no.2 entered into a series of buy and sell transactions for higher number of shares and finally transferred net 1,40,72,207 shares of NDTV to Noticee no. 3. This was carried out in off-market by way of inter-se transfers. SEBI further noted that instead of transferring requisite no. of shares directly, Noticee no. 1 and Noticee no. 2 entered into a series of buy and sell transaction which is not a usual practice. SEBI on investigation found that these inter-se transfers were actually framed to transfer beneficial interest in 30% shares of NDTV. Further SEBI on investigation also held that the loan amount of Rs 403.85 crore received from VCPL under Loan Agreements was actually a consideration to be paid to Noticee no.1 and Noticee no.2 by Noticee no.3 for transferring their stake.

4. **Warrants were never issued by RRPR to VCPL:** SEBI stated that in terms of Clause 6.1 of VCPL Loan Agreements, it is stipulated that the borrower shall issue convertible warrants, which were convertible into equity shares aggregating to 99.99% of share capital of borrower viz. Noticee no.3. Thus Noticee no.3 was under the obligation to issue convertible warrants to VCPL immediately after executing the loan agreement dated July 21, 2009. SEBI further stated that even if it is seen that warrants were never issued by Noticee no. 3 but it is pertinent to note that clause 13 of said loan

agreements stipulated consequences of default by way of breach of terms and conditions of the agreement by promoters or borrowers. As per these conditions if there was no issue of warrants, VCPL should have demanded back the loan from RRPR (Noticee No. 3). So SEBI held that even after 10 years of execution of agreements and despite the said default by Noticees, pre-payment has inexplicably not been triggered, which reinforces a thought that so called loan was never planned to be repaid and amount received was consideration for sale of their substantive stake in NDTV to VCPL.

5. **No breach of Fiduciary Duty:** SEBI stated that Loan Agreements are still in force and have not been renounced by VCPL. This shows that Noticee no. 1 and 2 have already placed their contractual obligations with VCPL above their fiduciary obligations as Directors of NDTV. SEBI further stated that terms of Loan Agreements itself states that decisions on all vital matters are contingent on the affirmative consent of VCPL. This also shows that Noticee no.1 and 2 (who are also Chairman and Managing Director, respectively) have put themselves under contractual obligations in executing key decisions. Such acts are in derogation of their fiduciary duty.

6. **NDTV was not a part of VCPL Loan Agreement:** SEBI stated that it is correct that NDTV was not a party to the agreement but the clauses of Loan Agreements clearly demonstrate that the scheme was devised in such a way that though NDTV was not a party to the said Loan Agreements, it had clauses which would significantly affect the functioning of NDTV. The Loan Agreements were devised in such a way that material and price sensitive information contained in these Loan Agreements would never be required to be disclosed to minority investors. This induced minority investors to trade in shares of NDTV in obliviousness about shift in control. These Loan Agreements were a part of colourable devise and were deceitful in nature. Hence it is clear that Noticee no.1 and Noticee no.2 have engaged in unfair trade practices.

Held by SEBI: Noticees have violated Section 12A(a) and (b) of SEBI Act, 1992 read with Regulation 3(a), (b), (c), (d), and 4(1) of PFUTP Regulations; and Noticees no. 1 and 2 are also in violation of Clause 49(1)(D) of equity listing agreement read with Section 21 of SCRA.

Penalty: Rs 25 crore payable jointly and severally by Noticees. Additionally, ₹ 1 crore each payable by Noticee no. 1 and Noticee no. 2.

Cases referred by Appellant: *Price Waterhouse vs SEBI [SAT Appeal no.8 of 2011-1 June 2011], Kashinath Dikshita vs Union of India & Ors (1986) 3 SCC 229. Rolta India Ltd vs Venire Industries Ltd 2000 (3) Mh. L.J. 700*

Respondent: *SEBI vs. Kishore Ajmera, 5, 2016 6 (SCC) 368, Kanyailal Baldev Bhai Patel vs Rakhi Trading Pvt Ltd (2018) 13 SCC 753, N. Narayanan vs Adjudicating Officer SEBI (2013) 12 SCC 152*