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CORPORATE LAWS

Case Law Update

Companies Act

World Crest Advisors LLP (appellant) VS Catalyst Trusteeship Ltd (respondent) & Ors. Division bench of Bombay High Court, Order dated 23rd June 2022

Facts of the case

- World Crest Advisors LLP (herein after referred as "World Crest"), and Dish TV India Ltd (herein after referred to as "Dish TV") belong to same group called Essel group, and World Crest has shareholding in Dish TV.
- Total 8 different entities (hereinafter referred as "borrowing entities") belonging to Essel group, had taken loan from Yes bank ltd. (hereinafter called "YBL").
- As a security for this loan, World Crest had pledged 26% shares of Dish TV held by it, with Catalyst trusteeship ltd. (hereinafter called "Catalyst"), a security trustee appointed by YBL, through a pledge agreement to which YBL was not a party.
- As per the pledge agreement, in the event of default by the borrower entities, Catalyst had a right to invoke the pledge and enter its own name as beneficial owner against the shares in question.
- The borrowing entities committed default and therefore as per the pledge agreement, Catalyst invoked the pledge and transferred the pledged Dish TV shares to itself. It got its name noted as the 'beneficial owner' with the depository. Thereafter, it further transferred the shares to YBL or constituted YBL as its nominee and as a result, it was YBL who exercised voting rights relating to the shares of Dish TV.
- Thereafter, Dish TV called its AGM on 27th September 2021, but postponed and rescheduled it to 30th December 2021 due to some disputes with YBL relating to calling of an EOGM requisitioned by YBL under section 100 of Companies act 2013.
- With respect to AGM scheduled on 30th December 2021, World Crest wrote an email to Dish TV on 8th December 2021 stating that due to the pledge agreement, its pledged shares of Dish TV are presently in custody of YBL

as security package for certain loans granted to Essel group until the said shares are sold or appropriated by YBL, but it still be allowed to vote at AGM since those shares continued to be a part of the security package. To this email, Dish TV replied 12th December 2021 that , as per the defined process, each of the shareholder will be entitled to vote on such shares which are held in its respective custody/demat account."

- As a result, World Crest filed a suit before Bombay High Court praying that exercise of voting rights by YBL be declared void and World Crest be allowed to vote at the above-mentioned AGM. But the Bombay High Court said that outcome of voting at AGM shall be subject to final order of the Court.
- Thereafter, Dish TV announced an EOGM to be held on 24th June 2022. Therefore, World Crest filed a separate petition praying injunction on YBL and Catalyst from exercising their rights at EOGM. But a Single Judge Bench of Bombay High Court ruled against World Crest and allowed YBL to vote at EOGM. Hence World Crest has preferred this appeal before the division bench of Bombay High Court.

Petitioner's contentions

- The case advanced by Ld. Counsel for World Crest as well as for Dish TV, is that both under the general law regarding pledges in Section 176 and 177 of the Contract Act, and following a recent decision of the Supreme Court in ***PTC India Financial Services Ltd vs. Venkateswarlu Kaki & Anr***[1] (hereinafter referred to as "PTC India case"):-
- Catalyst can transfer the pledged shares to its name but only for the limited purpose of holding them safely until they are redeemed, sold (after notice to World Crest) or for the purposes of Catalyst's recovery suit.
- Under no circumstances does Catalyst, as a pledgee, acquire general property in the shares sufficient to allow it to either
  - (i) further transfer the shares or make a nomination in favour of anyone in regard to those shares; or
  - (ii) exercise any rights emanating from those shares, such as voting at a general meeting of Dish TV.
- They further stated that, any such full-blooded transfer of all rights of 'general property' by Catalyst to itself (and certainly to YBL) is a sale-to-self, forbidden by the Contract Act.
- They also said that it is not permissible for World Crest itself as the pledgor-shareholder and Catalyst as the pledgee to enter into a contract giving Catalyst, in its capacity as a pledgee, such full proprietary, ownership, dispositive and general property rights in the pledged shares.

Respondent's contentions

Ld. Counsel for YBL argued that:

- Once Catalyst, as the pledgee, is shown as the beneficial owner of the shares,

1. 2022 SCC OnLine SC 608.

it exercises all rights as a shareholder of Dish TV. Indeed, once this change happens, only Catalyst can exercise those rights.

- There is no concept of a 'beneficial owner with restricted rights' for the purposes of the Companies Act, 2013 or any other law relating to shares and shareholdings. It is the other way around: none except the beneficial owner can exercise those rights.
- There is nothing in Contract Act or the above-referred PTC India case to suggest that there is such a restriction on the rights of beneficial owner.
- There is no prohibition in the Contract Act or above-referred PTC India case that prevents the parties from entering into a contract (or restricting the rights of the World Crest and Catalyst to enter into a contract) that permits a transfer by Catalyst of the shares — but without affecting a sale-to self, although a pledgee cannot sell the pledged security to itself.

Held

The Court observed that:

- Both sides have relied extensively on the above referred recent decision of the Supreme Court in PTC India case.
- PTC India restates long-standing law on pledges; it does not re-write it.
- PTC India's focus was in fact on Regulation 58(8) of SEBI (Depositories and Participants) Regulations 1996, and whether this created any new rights or obligations and specifically whether it changed the law under Sections 176 and 177 of Contract Act, 1872. The Supreme Court held that it did not change.
- Therefore, the law on pledges is, even after PTC India case, exactly as it stood before; as it stood at the date of the institution of the suit by World Crest; and as it stood when the pledge agreement was entered.
- Even in the pre-Regulation 58(8) period, a pledger could not contract to give the pledgee voting rights in the pledged shares.
- The Court said that it seems to us that World Crest's case however long on legal argumentation is remarkably short on equity. World Crest refuses to redeem the pledge. The law is clear that it cannot, without Catalyst's express approval, compel a sale of security. Catalyst is not bound to sell the security. It may do so. It may also file for recovery. For either case, it must record itself as the beneficial owner. There can be no quarrel with this. But, at the same time, World Crest contends that the security should count for nothing. The Court once again read the relevant clause in the pledge agreement which said "In consideration of the Lender(s) having lent ….., the Obligors hereby confirm that for securing the due payment, repayment or reimbursement, as the case may be, of the Secured Obligations, each Pledgor; …(b) as an owner of the Securities, *pledges all of its rights (including voting rights in or rights to control or direct the affairs of the Company),* title and interest in and to the Securities.

The Court further said that we are being asked to infer that the recording of Catalyst's name under Regulation 58(8) as the beneficial owner results in it having some severely curtailed rights as a beneficial owner. We are asked to hold - prima facie - that World Crest is not bound by the terms of the bargain it struck as a part of this pledge agreement. We find it difficult to accept this proposition.

We find it impossible to fault the decision of the learned Single Judge. He correctly refused to exercise the discretion vested in him.

The Appeal has no merit. It deserves to be dismissed. It is. No costs.

SEBI

Order of Adjudicating Officer of Securities and Exchange Board of India
Name of the Case: In the matter of Dish TV India Ltd (hereinafter referred to as "**DTL**" or "**the Company**")

Facts of the case

1. The present proceedings emanate from an interim order cum show cause notice dated **March 7, 2022** (hereinafter referred to as "**SCN**"), passed by the Securities and Exchange Board of India (hereinafter referred to as "**SEBI**") *inter alia* against Mr. Bhagwan Das Narang, Independent Director, Mrs Rashmi Agarwal, Independent Director, and Mr Shankar Aggarwal, Independent Director **['Noticees']** wherein it was *prima facie* found that the Noticees were in violation of the provisions of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as "**SEBI Act, 1992**") and the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (hereinafter referred to as "**LODR Regulations**")

2. It all started when certain entities belonging to the Essel Group (hereinafter referred to as "**Borrowers**") availed loans of INR 5,270 Crores between 2015 and 2018 from Yes Bank Limited (hereinafter referred to as "**YBL**"). A total of 47,19,13,990 shares of DTL (amounting to 25.63% of total shareholding of DTL) were pledged in favour of YBL by two promoter entities of DTL, namely, World Crest Advisors LLP (hereinafter referred to as "**WCA LLP**") and Direct Media Distribution Ventures Private Limited (hereinafter referred to as "**DMDVPL**") (hereinafter collectively referred to as "**Pledgors**"), as security for the said loans. In this regard, Deeds of Pledge were executed between the Security Trustees of YBL (Catalyst Trusteeship Services Limited and IDBI Trusteeship Services Limited) and the Borrowers. Between May and July 2020, the borrowers defaulted on the loans, and the Security Trustees invoked the pledge. Subsequently, the Security Trustees took steps to get the pledged shares transferred in their own names or in the name of YBL. Aggrieved by the above, WCA LLP filed a Commercial Suit No. 29569 of 2021 (hereinafter referred to as "**Suit**") before the Hon'ble Bombay High Court alleging that YBL's shareholding in the *Company* is bad in law. WCA LLP *inter-alia* prayed for an *ad-interim* injunction restraining YBL from voting at the AGM of the Company (which was scheduled on December 30, 2021). WCA LLP also prayed for postponement of the AGM and/or

stay the effect and implementation of decisions taken in the said AGM.

3. The Hon'ble Bombay High Court, vide an order dated December 23, 2021, rejected the interim reliefs sought by WCA LLP and directed that the *"result/outcome of the AGM to be held on 30th December, 2021, will abide by the decision in the above Interim Application."* **Pursuant to this Dish TV India Ltd ('DTL'/'the Company')** held the AGM but **did not submit the voting results of Annual General Meeting of DTL held on December 30, 2021** to the stock exchanges**.** DTL made a disclosure to stock exchanges, that it had requested the Scrutinizer to place all the information relating to e-voting in the AGM along with his Report in a sealed cover and hand the same over to the Company Secretary and Compliance Officer of the Company. It was stated that the same shall be placed before the Hon'ble Bombay High Court for further directions. The Company informed that it had also moved an application to place the voting results in a sealed cover before the Hon'ble Bombay High Court.

4. Thereafter SEBI received a complaint dated December 31, 2021 from YBL *inter-alia* requesting SEBI to ensure that the *Company*, being a listed entity, forthwith discloses the results of the AGM in terms of the requirement under Regulation 44(3) of the LODR Regulations. After examining the issue, SEBI issued an Advisory letter dated January 17, 2022 to DTL **("First Advisory")** advising it to disclose the voting results/outcome of the AGM held on December 30, 2021, clearly mentioning the directions of the High Court, immediately. SEBI also asked the Company to disclose the First Advisory to stock exchanges. It was noted that the Company did not disclose the First Advisory to stock exchange. DTL replied to the First Advisory, vide its letter dated January 18, 2022, stating that the issue of declaration of results of the AGM was *sub-judice* before the Hon'ble Bombay High Court by virtue of IA No. 121 of 2022 filed by the *Company* and IA No. 376 of 2022 filed by YBL, and requested SEBI to suspend the Advisory pending a decision in the aforesaid Interim Applications.

5. SEBI examined the reply of the Company and the Order passed by the Hon'ble Bombay High Court vide its order dated December 23, 2021. It was observed that there was no specific restraint imposed by the Hon'ble Bombay High Court on declaring the results of voting of the above noted AGM. The Hon'ble Bombay High Court had only directed that the result/outcome of the AGM to be held on December 30, 2021, *will abide by the decision in the above Interim Application, and rejected any ad-interim relief*. The Hon'ble Bombay High Court had not issued any directions to prohibit the Company from disclosing the outcome of the AGM. Hence, SEBI issued another letter dated February 9, 2022 (hereinafter referred to as "**Final Advisory**"), drawing the attention of the Company to its statutory obligation towards shareholders and other stakeholders and its failure to act in compliance with the provisions of Regulation 44(3) of the LODR Regulations. The Company was once again advised to immediately

disclose the voting results of the AGM held on December 30, 2021. Further, the Company was also informed that continuing non-compliance shall result in initiation of appropriate enforcement action against the Company. The Company was also advised to disclose the Final Advisory to the Exchanges for dissemination of the same to investors. The said letter was sent to the Company by way of an email dated February 09, 2022 at 06:57:00 PM in the evening. Thereafter, DTL submitted a letter dated February 10, 2022 to SEBI, in reply to the Final Advisory reiterating that the issue of declaration of AGM results was pending with the Hon'ble Bombay High Court. DTL requested SEBI, to await the outcome of the proceedings pending before the Bombay High Court. The Company, however, disclosed the Final Advisory to the Stock Exchanges on February 10, 2022 at 9:58:36 PM.

6. SEBI has now, in the SCN dated March 7, 2022, alleged that the Company had delayed the disclosure, knowing fully well that there was no such stay/ direction in operation, which would prohibit the *Company* from disclosing the outcome of the above AGM held on December 30, 2021. The SCN also noted that subsequently, the Hon'ble Bombay High Court clarified its position in its order dated February 17, 2022 in IA No. 376 of 2022, making the following observations:

> "*Mr. Khambata finds that the reason for delay in declaring of the results is said to be pendency of Interim Application (L) no. 29574 of 2021 and defendant no. 3 has claimed that the matter is sub-judice. It is clarified that pendency of the above two Interim Applications have no bearing on the requirement reiterated by SEBI…*"

SEBI further alleged that the Company did not disclose the voting results inspite of advisories being issued by SEBI and above clarification from Hon'ble Bombay High Court. SEBI also noted that as on the date of issue of SCN, there is a delay of 68 days in submission of voting results. SEBI directed the Compliance Officer of DTL to disclose the voting results within 24 hours of receipt SCN. SEBI further ordered freezing of demat accounts of Directors and Compliance Officer of DTL till the time voting results of the AGM held on December 30, 2021 are announced to stock exchange or till further orders, whichever is earlier.

7. SCN further called upon the Noticees to show cause as to why further appropriate directions under the provisions of Sections 11(1), 11(4) and 11B (1) of SEBI Act, 1992 should not be issued against them and also why appropriate penalty should not be imposed in terms of Section 11B(2) read with 11(4A) of SEBI Act, 1992 read with Sections 15A(b) and 15HB of SEBI Act, 1992 for the aforementioned alleged violations of law committed by them.

8. The Company, the compliance officer and non-independent directors have filed settlement applications with SEBI and those are pending with SEBI, and hence the SCN is address to the independent directors of the Company only.

Charges levied

1. Board of Directors of the Company was *prima-facie* in violation of the provisions of Regulations 4(2)(f)(ii)(6), 4(2)(f)(ii)(8), 4(2)(f)(iii)(2), 4(2)(f)(iii)(3), 4(2)(f)(iii)(6) read with 17(3) of LODR Regulations. The Board of Directors of the Company was also *prima-facie* in violation of the Clauses 4.1, 4.4, 5.1, 5.2 and 5.11 of the Code of Conduct for Directors and Senior Management (hereinafter referred to as "Code of Conduct"), as available on the website of the Company, framed pursuant to Regulation 17(5) of the LODR Regulations, read with Regulation 26(3) of the LODR Regulations. The Independent Directors on the Board of the Company were also *prima-facie* in violation of the provisions of Clauses 1 and 2 of Schedule A of the Code of Conduct read with Regulation 26(3) of the LODR Regulations, wherein additional duties of independent directors were prescribed under Schedule IV of Companies Act, 2013.

Arguments made by Noticees (Independent directors)

Noticees of the Company cannot be held liable for any alleged misconduct of the Company unless it is through a Board Process

The Noticees claimed that, they being non-executive directors, cannot be held liable for any alleged misconduct of the Company unless it is through a Board Process with the active consent of the Directors under Section 149(12) of the Companies Act, 2013. Noticees further submitted that:

a. A Board Meeting was fixed for February 24, 2022 for consideration and approval of the Un-Audited Financial Results of the Company for the quarter ended on December 31, 2021 and just before commencement of the said Board Meeting, they were informed about the Advisories from SEBI..

b. It was the first time they were informed of the SEBI Advisories. They were also informed that the Management has already replied to SEBI vide their letters dated January 18, 2022 and February 10, 2022 and was awaiting a final response. The Management also elaborated that this was done in line with the legal advice received.

c. The Independent Directors advised the Management that any further communication from SEBI be immediately brought to the attention of the Independent Directors and no further reply be sent without their consent.

d. The Board felt that in view of the reply already sent by the Management of the Company in response to the Advisories of SEBI, it would be prudent to await the final decision of SEBI.

e. Further, the Independent Directors, after application of mind, and in discharge of their fiduciary duties, and in view of the explanation given by the Management, felt that since replies to SEBI have already been issued, it would be prudent to await the final response of SEBI.

f. The Independent Directors however asked the Management to examine the Advisories legally and act accordingly. The order of the Hon'ble Bombay High Court dated December 23, 2021 and February 17, 2022 (as corrected on February 21, 2022) were never discussed

in the Board. The Independent Directors were never aware of the loan/borrowing taken by the promoter/promoter group and/or the borrowing entities as referred to in the SCN.

g. It is a well-established principle that the liability of Independent Directors is extremely limited. The Noticees relied on judgments like *V. Selvaraj v. Reserve Bank of India*, 2019 SCC OnLine Mad 38930, *S.M.S Pharmaceuticals Ltd. v. Neeta Bhalla and Ors.*, [2005] 8 SCC 89, *Seema Khandelwal, In re, 2020 SCC OnLine SEBI 55, Sayanti Sen v. Securities and Exchange Board of India*, 2019 SCC OnLine SAT 132. and Circular dated March 2, 2020 issued by the Ministry of Corporate Affairs of the Government of India in support of their submissions in this regard.

Observations by SEBI Whole Time Member on the arguments put forth by Noticees:

Noticees of the Company cannot be held liable for any alleged misconduct of the Company unless it is through a Board Process

a. SEBI stated that Regulation 6 read with Regulation 17(8) of LODR Regulations provide that the matters related to disclosure are to be overseen, mainly by the Company Secretary and by Whole Time Directors. Further as per Regulation 24(2) of LODR Regulations which requires the listed entity to submit, quarterly compliance report on cooperate governance, states that the same shall be signed by either compliance officer or CEO. SEBI thus noted that LODR Regulations, for practical purposes, impose the burden of compliance of matters relating to filing and disclosure mainly on the compliance officer/CEO - who are KMPs and/or whole-time directors of the company and involved in the day to day management of the company. In this SEBI accepted the submissions of Noticees that they were informed of the SEBI Advisories (dated January 17, 2022 and February 9, 2022) on February 14, 2022, just prior to the commencement of the Board Meeting.

b. However, SEBI further stated that it is not correct to say that knowledge of independent directors must be the one acquired through the board processes. The knowledge of the independent directors could be acquired through any reliable and credible sources including public disclosures available on the website of the stock exchanges where shares of the company are listed as disclosed by the company.

c. SEBI noted that SEBI's First Advisory was not disclosed by DTL to the Exchanges. As a result, the fact that SEBI had issued such an advisory was not in the public domain. The material available on record, does not suggest that the Noticees were otherwise aware of the First Advisory issued by SEBI. The Final Advisory was disclosed by DTL to the exchanges, and thereafter, the same was widely reported by various news outlets between February 11-12, 2022, i.e. couple of days before the Board Meeting held on February 14, 2022.

d. The SCN and facts and circumstances of the case do not show whether the replies of the Company dated January 18, 2022 and February 10, 2022 to SEBI and disclosure to the stock

exchanges on February 10, 2022 was done after deliberation with independent directors and the facts do not indicate any complicity of the Independent Directors with respect to the disclosures under Regulation 44(3) of the LODR Regulations and the Advisories issued by SEBI. Thus, no omission to exercise due diligence can be attributed to the independent directors in the facts and circumstances of the case.

e. Regarding order dated February 17, 2022 of the Hon'ble Bombay High Court, the SEBI Whole Time Member noted that the Independent Directors have stated that they were not aware of the aforesaid order. Unlike the information pertaining to the filing of the Suit by WCA LLP and order dated December 23, 2021 passed therein, the order dated February 17, 2022 was not disclosed by the Company to the Exchanges. The SEBI Whole Time Member found that the material available on record does not indicate that the Noticees herein were otherwise aware of this order and having regard to discussions recorded in above paras, failure to inform the said order to the stock exchanges, is not attributable to these Noticees, in the facts and circumstances of the case.

f. SEBI concluded that Independent Directors of the Company cannot be held liable for any alleged misconduct of the Company unless it is through a Board Process with the active consent of the Directors. The phrase "attributable through Board processes" appearing in this section warrants special attention and must not be considered merely ornamental. In this regard, in the present case the decision to not disclose the AGM results, was not taken with the knowledge of the Independent Directors attributable through Board processes, or with their consent or connivance and therefore, no liability can be affixed on the Independent Directors.

Held by SEBI: Matter disposed off without penalty

Cases quoted by Noticees: ***V. Selvaraj vs. Reserve Bank of India, 2019 SCC OnLine Mad 38930, S.M.S Pharmaceuticals Ltd. vs. Neeta Bhalla and Ors., [2005] 8 SCC 89, Seema Khandelwal, In re, 2020 SCC OnLine SEBI 55, Sayanti Sen vs. Securities and Exchange Board of India, 2019 SCC OnLine SAT 132.***

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"All truth is eternal. Truth is nobody's property; no race, no individual can lay any exclusive claim to it. Truth is the nature of all souls."

— *Swami Vivekananda*