BEFORE THE SECURITIES APPELLATE TRIBUNAL MUMBAI

Appeal No. 48 of 2006

Date of decision : 21.10.2008

M/s. Guru Teak Investments (Mysore) Pvt. Ltd. …… Appellant

Versus

Securities and Exchange Board of India …… Respondent

Mr. Vineet Jagtap Advocate for the Appellant.
Mr. Kumar Desai Advocate with Mr. Amit Survase and Ms. Rozmin Lakhani Advocates for the Respondent.

Coram : Justice N.K. Sodhi, Presiding Officer
Utpal Bhattacharya, Member

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

This is one of the oldest appeals pending before the Tribunal. It was taken up for hearing on March 29, 2007 when the arguments were partly heard. When we were adjourning the case for the next day, a very strange request was made seeking an adjournment on the ground that the senior counsel from Bangalore had to come to address further arguments on behalf of the appellant. Having regard to the fact that the interest of very large number of investors was involved and lest there was any miscarriage of justice, we acceded to the request and adjourned the case to April 5, 2007. After getting the case adjourned, the appellant filed a writ petition in the High Court of Karnataka challenging the definition of "networth" as contained in the Securities and Exchange Board of India (Collective Investment Schemes) Regulations, 1999 (hereinafter referred to as the Regulations). Further proceedings before the Tribunal were stayed. The case was then being adjourned from time to time in view of the stay order granted by the Hon'ble High Court. The writ petition has since been dismissed by a learned single Judge on July 8, 2008, The Securities and Exchange Board of India (for short the Board) then filed Misc. Application on 10.9.2008 for getting the case listed and attached a copy of the order passed by the High Court. The appeal was then listed for hearing on September 26, 2008 on which date the learned

counsel for the appellant sought an adjournment on the ground that he was under the impression that the case had been listed for directions. We adjourned the case to October 20, 2008 for final disposal. The case came up for hearing yesterday and we heard counsel for the parties. We were about to dictate the order when court time was over and we adjourned the matter for today. Today, the learned counsel for the appellant states that his request for an adjournment be first considered before dictating the order. In the circumstances stated above, we are not inclined to adjourn the matter and having heard the learned counsel for the parties, we are proceeding to dictate the order.

2. M/s. Guru Teak Investments (Mysore) Pvt. Ltd. is the appellant before us. It is a Collective Investment Management Company and is stated to be operating as many as ten collective investment schemes. Since the schemes were being operated by the appellant prior to the coming into force of the Regulations, those were existing collective investment schemes within the meaning of the Regulations and were governed by the same. The appellant was required to make an application to the Board for the grant of provisional certificate(s) of registration of the schemes. Having made such an application, the Board granted a certificate of provisional registration of the schemes on July 9, 2001 subject to the following conditions :-

"(a) Company shall get existing schemes rated by a Credit rating agency within one year from the date of grant of Provisional Registration;

(b) The company shall not launch any new scheme or raise money from the investors under the existing scheme;

(c) Company shall get the existing schemes audited by an auditor within one year from the grant of Provisional Registration;

(d) Company shall get the existing schemes appraised by appraising agency within one year;

(e) Company shall create trust and appoint trustees as specified in chapter IV of Regulations within one year;

(f) Company shall comply with accounting and valuation norms as provided in Part II of the ninth schedule of the Regulations within one year;

(g) Company shall meet a minimum net worth of Rs. One Crore within one year and will increase the same by Rs. One Crore each within two, three, four & five years;

(h) Company not to dispose of the Scheme Property except for meeting obligation arising under the offer document;

(i) Company to comply with conditions in Regulation 11 of the Regulations and to inform SEBI regarding any material change;

(j) Company to comply with the code of conduct and all other guidelines issued by the SEBI;

(k) Company to maintain books and documents as per Regulation 40 of the Regulations;

(l) Company to abide by Regulations as amended from time to time;"

According to the Board, most of the conditions specified in the aforesaid order have not been complied with by the appellant despite several opportunities having been granted to it for the purpose and, therefore, by order dated 8.2.2006 the appellant company was directed to wind up the schemes and make payment to the investors as per the provisions of Regulation 73 of the Regulations. It is against this order that the present appeal has been filed.

3. When this appeal came up for admission on February 28, 2006 we stayed the operation of the impugned order and also the direction given to the appellant to repay the investors. The appellant was, however, directed to prepare an information memorandum as contemplated by Regulation 73 of the Regulations and send a draft thereof to the Board and it was open to the latter to make suggestions if it so wanted within two weeks from the date of receipt of the information memorandum. The suggestions, if any, that were to be made by the Board were required to be incorporated in the information memorandum before the same was sent to the investors. The appellant company was also directed to obtain positive consent of the investors in terms of said Regulations and after the receipt of the views of the investors, the appellant was required to prepare a summary in a tabulated form for further perusal of this Tribunal if it became necessary. The appellant company was directed not to mobilize any further funds from the investors till further orders.

4. We have heard the learned counsel for the parties. The learned counsel appearing for the respondent Board has urged that the appellant company failed to comply with most of the conditions enumerated in the order of July 9, 2001 granting provisional registration and is, therefore, not entitled to the registration of the schemes under the Regulations and that the Board was justified in directing the appellant to wind

up those schemes and repay the amounts to the investors. The learned counsel for the appellant, on the other hands, contends that most of the conditions enumerated in the order of provisional registration have been complied with. He very fairly conceded that the company has not been able to appoint till date the trustees as specified in Chapter IV of the Regulations and that it has not been able to meet the requirements of a minimum networth of Rs.1 crore within one year from the date of the order of provisional registration and it could not increase the same by Rs.1 crore each year within the next two, three, four and five years. In view of the admission made by the learned counsel for the appellant, it is clear that even though the appellant has created a trust it has not appointed the trustees who have to hold the assets of the schemes in trust for the benefit of the investors. We find from the records of the case that the land acquired by the company for plantation under various schemes stands registered in the names of the Managing Director, Directors and Advisory Committee members and have not been transferred to the Trust. We wonder how, under the circumstances, the schemes can be allowed to operate. The scheme of the Regulations is that different collective investment schemes shall be operated by the collective investment management company but the assets shall be held by the trustees for the benefit of the unit holders. Only such persons who are registered with the Board as debenture trustees under the Securities and Exchange Board of India (Debenture Trustees) Regulations, 1993 are eligible to be appointed as trustees of collective investment schemes. This apart, the company has not been able to meet with the requirement of minimum networth under the Regulations. The Board in the impugned order has referred to the points raised by the auditors of the appellant company which are as under:-

> "i the requirement of schemes being constituted in the form of a trust and appointment of trustees as per CIS Regulations has not been complied with.
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> ii. In deviation to the conditions stipulated at the time of grant of provisional registration, the company has been accepting Unit Capital from investors till March 2005.
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> iii. The regulations stipulate that none of the schemes shall be open ended and any scheme shall be kept open for subscription for a maximum of ninety days. Contrary to the requirement, all the schemes are open ended.
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> iv Each scheme shall be launched with trustees approval along with credit rating obtained from credit agency and appraisal from appraisal agency. Further, credit rating and appraisal

> functions are required to be performed continuously at the end of every financial year for all the schemes as per the regulations. These stipulations are not carried out with regard to all the schemes in operation."

The learned counsel for the appellant could not controvert the correctness of the observations made by the auditors of the company. From the issues raised by the auditors, it is clear that the company has been accepting unit capital from investors till March 2005. Regulation 69 of the Regulations clearly stipulates that no existing collective investment scheme shall launch any new scheme or raise money from the investors even under the existing scheme(s) unless a certificate of registration is granted to it by the Board under Regulation 10. Admittedly, a certificate of registration has not been issued to the appellant under Regulation 10. Despite this, the appellant company has been collecting funds from the investors and has collected a sum of Rs.53.52 crores during the period from 1.4.2000 to 31.3.2004 which is contrary to law and the conditions enumerated in the order granting provisional registration.

5. There is yet another reason why we are not inclined to allow the appellant company to continue to operate its collective investment schemes. In pursuance to the interim order passed by us, the appellant company issued information memoranda to all its investors in terms of Regulation 73 of the Regulations to ascertain their views whether they were willing to give positive consent to continue with the scheme(s). We have perused some of these information memoranda and find that the company has misled the small time investors who invested small amounts of Rs.1000/- each in different schemes. One of the schemes is B-25. The information memorandum pertaining to this scheme informs the investor(s) that he had invested a sum of Rs.1000/- and that the total amount payable on the date of the memorandum was Rs.1240/- and that if he were to continue with the scheme he would get 10 cubic feet of teakwood or an amount of Rs.25000/- (approximately) on the maturity date 27.11.2028 whereas the scheme is that the investors would get only 6 cubic feet or Rs.15000/- on maturity. Similar misleading statements have been found in some other information memoranda pertaining to other schemes as well. We are satisfied that these misleading statements had been made in the information memoranda only to lure the small time investors to remain invested in the scheme. These investors are mostly ignorant

villagers residing in the remote villages of the State of Karnataka and other states where the schemes are operating. Such being the conduct of the appellant company, we cannot but uphold the impugned order directing the company to wind up the schemes in accordance with the Regulations. The learned counsel for the respondent Board has also brought to our notice some of the suggestions which the Board had made on receipt of the draft information memorandum from the appellant which it failed to incorporate therein before sending the same to the investors. This again is a serious matter and the appellant company cannot be allowed to operate the schemes.

6. In view of what we have observed hereinabove, it is not necessary to deal with the other contentions raised on behalf of the respondent Board.

7. For the reasons recorded above, the appeal fails and the same is dismissed. The appellant will now wind up the schemes in accordance with the provisions of the Regulations and repay the investors in accordance with the provisions of Regulation 73. We make it clear that the appellant will send to its investors fresh information memoranda after getting the same vetted from the Board. As soon as the information memoranda are finalised and sent to the investors, the Board shall release the amount of Rs. 50 lacs lying with it together with interest accrued thereon to the appellant company to be utilised for repayment to the investors. The Board shall have its costs from the appellant which are assessed at Rs.25,000/-.

Sd/-
Justice N.K. Sodhi
Presiding Officer

Sd/-
Utpal Bhattacharya
Member

21.10.2008
bk and ddg/-