SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

Order under Regulation 13 of the SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulation, 2002 against M/s Keynote Corporate Services Ltd. in the matter of public issue by M/s Maha Chemicals Ltd.

CO/ 138 /ISD/09/2003

1.0 M/s Keynote Corporate Services Ltd. (hereinafter referred to as 'Keynote') is a merchant banker registered with The Securities and Exchange Board of India (hereinafter referred to as 'SEBI') under Certificate of Registration No. INM 000003606.

1.1 M/s Maha Chemicals Ltd. (hereinafter referred to as 'MCL') is a company incorporated under the Companies Act, 1956 and in the business of manufacturing zinc oxide. MCL came out with a public issue of 32 lakh equity shares of Rs.10/- each for cash at par. The issue opened on 04.04.1994 and closed on 07.04.1994. M/s PNB Capital Services Ltd. (hereinafter referred to as 'PNB Caps') and Keynote were the Lead managers to the issue and as per the inter-se allocation of duties as informed to SEBI, Keynote was responsible for marketing and for post issue activities at Mumbai. The shares were allotted on 09.06.1994 and listed on The Stock Exchange, Mumbai and Ahmedabad Stock Exchange.

1.2 An investigation by SEBI revealed that minimum subscription in the public issue was met by taking into account applications that were submitted after closure of issue i.e. late applications. It was also noted that the 90 day and 120 day reports were not submitted to SEBI.

2.0 In view of the above, vide order dated 22.03.2001 Chairman SEBI appointed an enquiry officer to enquire into the conduct of Keynote in the said public issue. The Enquiry Officer issued show cause notice to Keynote on 17.07.2001 advising them to furnish a reply to the allegation that Keynote had failed in discharging in a diligent manner , the responsibility undertaken by them and that thereby they had violated Regulation 25 and Code of Conduct of the SEBI (Merchant Banker) Regulations, 1992.

2.1 The Enquiry Officer submitted his report to SEBI on 18.12.2002 recommending that a penalty of suspension of the Certificate of Registration of a period of two months may be imposed on Keynote. In his report the enquiry officer found that Keynote have failed to exercise due diligence while acting as merchant banker in the public issue of MCL and thereby violated Clause 2 of the Code of Conduct specified in Schedule III and Regulations 13 and 25 of the SEBI (Merchant Banker) Regulations, 1992.

2.2 Pursuant to the submission of report by the Enquiry Officer, show cause notice dated 28.04.2003 was issued to Keynote advising them to show cause as to why the action recommended by the Enquiry Officer should not be imposed upon them. Keynote submitted their reply vide letter dated 13.05.2003 and also sought a personal hearing in this regard. Accordingly, personal hearing was granted by me on 12.06.2003 wherein Keynote appeared and also subsequently made further submissions vide their letter dated 11.07.2003.

2.3 In view of the above, I am satisfied that Keynote have been afforded adequate opportunity to make submissions and that the requirements of natural justice have been met. Therefore, I proceed further in the matter.

Consideration of Issues

3.0 I have considered the facts of the matter, report of the enquiry officer, submissions made by Keynote and other material on record. The following issues arise for consideration.

3.1 **Whether Keynote has failed to exercise due diligence as a merchant banker in the public issue of MCL and thereby violated Clause 2 of the Code of Conduct and Regulations 13 and 25 of SEBI (Merchant Banker) Regulations, 1992**.

3.1.1 I note that PNB Caps was the Lead Manager to the issue and they had obtained acknowledgement card dated 11.02.1994 from SEBI in this regard. Subsequently, MCL vide letter dated 01.03.1994 appointed Keynote also as Lead Manager and PNB Caps vide their letter dated 07.03.1994 informed SEBI about the same.

3.1.2 Keynote, in their reply dated 16.08.2001 to the Enquiry Officer had stated that alongwith the letter dated 07.03.1994, inter se allocation of duties between PNB Caps and Keynote was also enclosed. They had further submitted that in terms of the said allocation, the role of Keynote was restricted to certain aspects of marketing and joint responsibility in respect of post issue activities at Mumbai.

3.1.3 In this regard, I note that the Enquiry Officer in his report has observed that although Keynote furnished a copy of letter dated 07.03.03, it did not furnish a copy of the inter se allocation of duties. Further, the Enquiry Officer has also observed that during the investigations PNB Caps had taken a stand that post issue activities were the responsibility of Keynote and the post issue reports submitted by Keynote had been signed only by them and did not bear signatures of PNB Caps. The Enquiry Officer also observed that Keynote had never informed SEBI about the non co-operation by PNB Caps. In view of the above, I agree with the findings of the Enquiry Officer and find that Keynote was having responsibility of post issue activities.

3.1.4 I note that as post issue Merchant Banker, Keynote was responsible for finalization of basis of allotment, weeding of multiple applications, listing of instruments and for follow up with various agencies connected with post issue work such as registrars and bankers to the issue. I further note that SEBI vide circular dated 01.03.1993 had directed that a post issue merchant banker has to maintain close co-ordination with the Registrar to the Issue and arrange to depute its officers to the offices of various intermediaries at regular intervals after closure of issue so as to monitor the flow of applications from collecting bank branches.

3.1.5 I note that SEBI's investigations revealed that minimum subscription in the pubic issue of MCL was said to have been obtained by bringing in late applications which amount to 33% of the issue size. Of these late applications those accompanied by stock invests constituted 17% of the issue size. As post issue merchant banker it was a responsibility of Keynote to ensure that late applications were not taken into account while arriving at collection figures to compute subscription received and to ensure that the allotment was not made to the late applicants.

3.1.6 I also note that Keynote had failed to bring to the notice of SEBI or the stock exchange, the non receipt of explanation from MCL about substantial variation in collection figures. I also note that Keynote had failed to submit the 90 day and 120 day reports to SEBI.

3.1.7 In their reply dated 13.05.2003, Keynote has submitted that the said public issue was one of the first assignments undertaken by them after their registration as a Category I merchant banker. They further stated that in view of their past association with PNB Caps they were under the honest impression that PNB Caps being the named merchant banker would oversee the activities relating to allotment and listing since they (i.e. PNB Caps) were located in Ahmedabad. Hence, they have stated that the lapse on their part was unintentional and on account of faith reposed in the main merchant banker.

3.1.8 Keynote have also submitted that they have handled over 100 public issues and the number of takeovers since December 1993 and there have been no complaints against them except for the present complaint.

3.1.9 They further submitted that in order to inject a sense of accountability and responsibility on Merchant Bankers and with a view to ensure that the Merchant Bankers comply with various guidelines and circulars issued by SEBI a system of imposing penalty point was introduced by SEBI to the Merchant Banker and penalty provisions were contained in SEBI regulations. The areas of non compliance / defaults were characterized into four areas namely general, minor, major and serious defaults. The penalty points were awarded to the Merchant Banker based on type of default. In the case of MCL no penalty point was awarded for non submission of post issue reports. As the allotment in said issue was complete and equity shares were listed they were under a honest impression that these formalities have been completed by the other merchant banker.

3.1.10 I find that the explanation / submission of Keynote are not satisfactory. Admittedly Keynote have failed to carry out post issue activities such as submission of 90 day and 120 day reports. They have also failed to ensure that the late applications were not taken into consideration to arrive at the subscription received and such late applicants were not allotted shares.

3.1.11 I note that Regulation 25 of the SEBI (Merchant Banker) Regulations, 1992 (hereinafter referred to as merchant banker regulations) provides that :

> "The lead manager undertaking the responsibility for refunds or allotment of securities in respect of any issue shall continue to be associated with the issue till the subscribers have received the share or debenture certificates or refund of excess application money;
>
> Provided that where a person other than the lead manager is entrusted with the refund or allotment of securities in respect of any issue, the lead manager shall continue to be responsible for ensuring that such other person discharges the requisite responsibilities in accordance with the provisions of the Companies Act and the listing agreement entered into by the body corporate with the stock exchange.

3.1.12 I note that the Code of Conduct for Merchant Bankers mentioned in Schedule III of the Merchant Banker Regulation provides that :

"1. A merchant banker in the conduct of his business shall observe high standards of integrity and fairness in all his dealings with his clients and other merchant bankers.

2. A merchant banker shall render at all times high standards of service, exercise due diligence, ensure proper care and exercise independent professional judgement. He shall wherever necessary, disclose to the clients, possible source of conflict of duties and interests, while providing unbiased services."

Regulation 13 of the Merchant Banker Regulation provides that :

"Code of Conduct –

13. Every merchant banker shall abide by the Code of Conduct as specified in Schedule III."

In view of the above, I find that Keynote has violated Regulation 13 and 25 of the SEBI (Merchant Banker) Regulations, 1992 and Clause 2 of the Code of Conduct for Merchant Bankers.

3.1.13 I also note that Regulation 35 of the merchant banker regulations provides as under:

"Liability for action in case of default .

35. A merchant banker who –

(a) fails to comply with any conditions subject to which certificate has been granted.

(b) Contravenes any of the provisions of the Act, rules or regulation,

Shall be dealt with in the manner provided under the Securities and Exchange Board of India (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (hereinafter referred to as "Enquiry Regulations").

4.1 I note that the Enquiry Officer, who was appointed in terms of regulation 39(1) of the un-amended Merchant banker Regulations, 1992 on 22.03.2001 has submitted his report to SEBI in terms of Regulation 13 of the Enquiry Regulations on 18.12.2003. I further note that since the SEBI (Merchant Banker) Regulations, 1992 have been amended by the Enquiry Regulations w.e.f. 27.09.2002, penalty is to be imposed under Regulation 13 of the Enquiry Regulations.

4.2 A merchant banker holds a position of great trust and responsibility in any public issue and investors depend on the actions of the merchant banker for safeguarding of their interests. In the present case, Keynote has failed to exercise the diligence expected of them and their failure has resulted in the wrongful conclusion that the issue had received minimum subscription. I further note that the failure on the part of Keynote had resulted in late applicants being allotted shares in the public issue. In view of the above, I agree with the recommendation of the Enquiry Officer that the Certificate of Registration granted to Keynote be suspended for a period of 2 months.

5.1 In view of the above, in exercise of the powers conferred on me under Section 4(3) of the SEBI Act and Regulation 13 (4) of the Enquiry Regulations I hereby suspend the Certificate of Registration bearing INM 000003606 granted to Keynote Corporate Services Limited for a period of 2 months.

This order shall come into effect 21 days from date of the order.

G. N. BAJPAI

Date : 26th September, 03

CHAIRMAN

Place: Mumbai

SECURITIES AND EXCHANGE BOARD OF INDIA