

# SECURITIES AND EXCHANGE BOARD OF INDIA

## ORDER

**Under Section 11(4) and 11B of SEBI Act, 1992, read with Regulation 11 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 and Regulation 11 of SEBI (Prohibition of Insider Trading) Regulations, 1992.**

WTMO/30/IVD/3/04

### Background

- 1.1 Alliance Capital Mutual Fund (ACMF) is a mutual fund registered with SEBI. It has been sponsored by Alliance Capital Management Corporation of Delaware, USA, whose parent company is Alliance Capital Management LP (ACM), USA. Alliance Capital Asset Management (India) Ltd. (ACAML) is the Asset Management Company of ACMF. ACAML is the subsidiary of Alliance Capital (Mauritius) P Ltd. (ACMPL), whose parent is also ACM.
- 1.2 During mid January 2003, various news items appeared in the print media inter alia to the effect that:
  - ACM had decided to sell its stake in their Indian subsidiary.
  - Shri Samir Arora, the Fund Manager of the ACMF and his Research team would exit from it.
  - ACMF was facing redemption pressure.
  - The Assets Under Management (AUM) of ACAML had fallen by around Rs.1000 crores.
  - The prices of certain scrips such as Balaji Telefilms Ltd., United Phosphorous Ltd., Hinduja TMT Ltd., Digital Globalsoft Ltd. and Mastek Ltd. had fluctuated substantially consequent to the rumors and uncertainty created about the sale of stake of ACAML.

- ACM issued a press release on February 3, 2003 stating that they had completed the review of the strategic alternative for ACAML and they would retain their ownership in the ACMF.
- Following the decision of not pursuing the sale of stake by ACM, the prices of the aforementioned scrips bounced back.

- 1.3 In the above background, Securities and Exchange Board of India (SEBI), in the interest of investors, ordered on June 6, 2003, an investigation into the affairs of ACAML and more particularly to ascertain the violation, if any, of the provisions of the SEBI Act, Rules and Regulations made thereunder.
- 1.4 Investigation conducted till 09.08.2003 revealed that Shri Samir C Arora, Head-Asian Emerging Markets at ACMSL was taking all investment decisions of the equity and balanced schemes of ACMF and was also managing the Indian allocation of Asian Funds of ACM, besides allocations for some other Asian countries.
- 1.5 In the course of investigations, it transpired that when ACM decided to sell its stake in ACAML, Shri Arora had reached an understanding with Henderson Global Investors for the purchase of the stake of ACM in ACAML and that his actions / inactions seemed to have been calculated to bring down the valuation of ACMF. It was found that the conduct of Shri Arora was not in consonance with the high standards of integrity, fairness and professionalism expected of a fund manager. Further, the timing and manner of disposal of ACMF's entire holdings in Digital Globalsoft smacked of Shri Arora's dealing in the security while in the knowledge of unpublished price sensitive information. Thus, there was a prima facie case of insider trading in terms of SEBI (Prohibition of Insider Trading) Regulations, 1992, by Shri Samir C Arora. It was also observed that, Shri Arora being the fund manager at ACMF and FIIs/sub-accounts of ACM, was prima facie responsible for the non-disclosures and wrong disclosures under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 and SEBI (Prohibition of Insider Trading) Regulations, 1992.

### Interim Order

- 2.1 In view of the aforesaid prima-facie findings of SEBI against Samri C. Arora and since he was in the process of setting up a new asset management business in India, there was an urgent need to take an emergent action to restrain Shri Samri C. Arora perpetrating/repeating his aforementioned conduct to the detriment of safety and integrity of the securities market and interests of the investors. A preemptive interim Order dated August 9, 2003 was, therefore, passed by me directing Shri Samir C Arora not to buy, sell or deal in securities, in any manner, directly or indirectly, till further orders.
- 2.2 In consonance with the principles of natural justice and the provisions of Section 11(4)(b) of SEBI Act, 1992, Shri Samir Arora was given an opportunity to file objections, if any, to the said Order within a period of 15 days from the date of the Order and also an opportunity of personal hearing, if he so desired, at 11:30 a.m. on August 28, 2003.
- 2.3 Pursuant to the said Order, Shri Samir C. Arora filed his objections through his Advocates on August 27, 2003. He also inspected all the relevant documents and attended the post decisional hearing on August 28, 2003. During the hearing Advocates of Shri Samir C. Arora made detailed submissions. After duly considering the submissions, the Order dated August 9, 2003, was confirmed by an Order dated 24.9.2003 directing Shri Samir C. Arora not to buy, sell or deal in securities, in any manner, directly or indirectly, till further orders. The investigating officer was also directed to complete the investigation expeditiously.

### Appeal before SAT

- 3.0 Aggrieved by the aforesaid Order, Shri Samir C. Arora filed an appeal no.134/2003 dated 09.10.2003 before the Hon'ble Securities Appellate Tribunal

(SAT). Even before SAT could hear his case, Shri Samir C Arora, filed a Writ Petition no. 2693 of 2003 in the Hon'ble High Court of Mumbai for remedy, on the grounds that the SAT was not fully functional and that there was a vacuum. During the hearing Union of India informed the Hon'ble High Court that the hearing was fixed for December 15, 2003 and by that time Tribunal will be functional. In view of the said statement the petitioner sought leave of the Court to withdraw the petition. Accordingly, the Hon'ble High Court has dismissed the writ petition as withdrawn. Thereafter, SAT heard the appeal and vide its interim order dated January 12, 2004 refused to grant Shri Samir C. Arora any interim relief in the matter and directed SEBI to make all efforts to pass the final order by February 28, 2004 and, in any case, to stick to the deadline of March 31, 2004.

#### Show Cause Notice

- 4.1 On completion of the investigation, a detailed showcause notice dated 20.02.2004 was issued to Shri Samir C Arora, citing facts, figures and circumstances, and alleging, inter-alia to the following effect:
- 4.2 The chain of cited events indicated that Shri Samir C Arora played a pivotal role in thwarting the stake sale plans of the ACM and his conduct and actions/inactions were with a selfish motive and contributed to the large scale redemption of the units of the fund. The large scale redemptions by the investors, the steep fall in the Asset Under Management (AUM) of ACMF and the resultant fall in Net Asset Value (NAV) of the schemes caused huge losses to the investors.
- 4.3 Shri Samir C Arora's participation in the bidding was in apparent conflict with his role as fund manager of ACMF. As a Fund Manager it was his responsibility to act for the benefit of the unit holders. However, in contrast, in his role as a bidder his interest was to acquire the fund at the cheapest possible price. In order to achieve the said objective he had by his actions/inactions, let the AUM fall, knowing that the valuation of the AMC would depend on AUM and in the process he had placed himself in a position of conflict of interest and compromised his fiduciary responsibility to the unit-holders and the sponsor. His conduct was

detrimental to the interest of investors and the orderly development of the securities market.

- 4.4 ACMF and the ACM along with the sub-accounts were holding significant quantity of the paid up capital of the scrips namely; Digital Globalsoft Limited (DGL), Balaji Telefilms Limited (BTL), Mastek Limited (Mastek), Hinduja TMT Limited (HTMT) and United Phosphorous Limited (UPL). The said five companies had high promoter holding and low floating stock as the promoter holding in each of the 5 said companies ranged between 33% and 58% as on December 31, 2002. The trading pattern in the said five scrips indicated that Shri Samir C Arora had indulged in manipulative transactions, inter alia, with the intent to artificially inflate/depress the prices of the scrip, to create false / misleading appearance of trading in the scrips in various scrips over a period of time and thus violated Regulation 4(a), 4 (b), 4 (c) & 4 (d) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995.
- 4.5 Shri Samir C Arora had appeared in the media and made discretionary comments on the investment potential or otherwise of those companies wherein the fund managed by him had invested in large proportions. His interview to Business Standard dated May 5, 2003 regarding the business prospects of DGL (wherein funds managed by him were holding about 4.45% of the equity) was an instance. In the interview with Business Standard in response to a query, “What is your allocation to tech stock and how do you find the valuations?”, he had, inter alia, replied “Digital Globalsoft – as per market rumours – may merge with HPISO in India, which will make it the sole subsidiary of a USD 70 billion plus IT company and therefore, be the obvious beneficiary of all the business that the parent can send to India, plus its normal business”. Soon after making such a positive statement about the prospects of DGL on account of the impending merger, he had sold, in consecutive trading days beginning May 8, 2003, all the shares held by funds under his management. Thus he had made a misleading statement with a

view to influencing the market price of DGL and thereby violated the provisions of Regulation 5 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995.

- 4.6 Being the Fund Manager, Shri Samir C Arora was aware of the combined holdings of ACMF, ACM (ultimate sponsor of the Mutual Fund and SEBI registered FII) and its FII / sub-accounts in various scrips, who all were PACs. He did not report ACMF, ACM and FIIs sub-accounts about their combined shareholding in various companies which resulted in non-disclosures/ wrongful disclosures under Regulation 7 of SEBI (SAST) Regulations 1997 and Regulation 13 of SEBI (Prohibition of Insider Trading) Regulations 1992. This had resulted in the failure of the Mutual Fund to make the requisite disclosures.
- 4.7 Shri Samir C Arora as Head – Asia Emerging Markets of Alliance Capital Management (Singapore) Ltd. was solely taking all investment decisions of the equity and balanced funds of ACMF and the Indian allocation of ACM and their FII and sub-accounts. In view of this, he was aware of the combined holdings of ACMF and PACs. SEBI (SAST) Regulations cast an obligation on the acquirer to disclose their combined holdings along with that of PACs to the respective target companies. He failed to advise the acquirer (i.e. ACMF) about the holdings by PACs to enable the ACMF to make the requisite disclosures as required by the said SEBI regulations.
- 4.8 Thus, Shri Samir C Arora's action/inaction had resulted in the failure of ACMF and PACs to comply with relevant SEBI regulations and consequently he had aided and abetted the violation of Regulation 7 of SEBI (Substantial Acquisition of shares and Takeovers) Regulations, 1997 and Regulation 13 of the SEBI (Prohibition of Insider Trading) Regulations, 1992. His conduct was, therefore, detrimental to the interest of investors and the orderly development of the securities market.

4.9 As on May 7, 2003 the funds managed by Shri Samir C. Arora together held 14,66,140 shares of DGL constituting about 4.45% of the total paid up capital of the company. The said shares had been held by the funds managed by him since February 2001. The funds combined holding reached upto 9.5% of the paid up capital of DGL in September 2002. He sold the entire holding of the funds managed by him in DGL in four consecutive trading days starting from May 8, 2003 based on unpublished price sensitive information pertaining to the de-merger of HP-ISO into DGL. The same was evident, inter alia, from the following:

- On April 10, 2003 the funds managed by him together held 14.66 lacs shares constituting 4.45% of the paid up equity capital of DGL.
- There were no transactions in the scrip of DGL by the funds managed by him since April 11, 2003.
- In an interview to Business Standard dated May 5, 2003 he had given favourable opinion regarding the business prospects of DGL consequent to the proposed merger with HP-ISO.
- Thereafter, beginning May 8, 2003 i.e. one day after the independent valuer submitted the valuation report to DGL, he off-loaded entire shareholding in DGL in four consecutive days.
- The reasons recorded for the sale inter alia include 'Event risk from tomorrow's announcement' which obviously referred to the merger ratio to be announced, which, he perceived, will be unfavourable to the shareholders of DGL.
- The agenda papers for the board meeting on May 12, 2003 did not have any mention of the discussion on the de-merger ratio. The intimation given by DGL to the stock exchanges regarding the proposed board meeting did not indicate that the issue of de-merger ratio would be taken up at the board meeting on May 12, 2003; The valuer had indicated that the sealed envelope containing the de-merger ratio should be opened only at the board meeting of the company scheduled to discuss the de-merger ratio.

- The commencement of sale since May 8, 2003 was significant considering that the valuer submitted their valuation report on May 7, 2003. Also, the hurry shown by ACMF to dispose off its holdings by May 12, 2003 was significant considering that DGL's board meeting was held on May 12, 2003 and one of the agenda items was 'Integration Related Items'.
- Shri Som Mittal, President and CEO of DGL knew him for the past 5-6 years.
- Shri Samir Arora and his analysts had the practice of making regular visits and interaction with the management and senior officials and they used to discuss the performance and future plans of the companies in which they invest.
- The funds managed by him were the single largest shareholder group of DGL after Compaq Computer Holdings Ltd. The funds were holding nearly 10% of the total paid up equity capital of DGL for several months and therefore ACM had a special interest in DGL and vice versa.
- The senior management team of DGL who were interacting with the valuer could easily estimate the likely de-merger ratio which was a price sensitive information.
- The fact that the board meeting of DGL on May 12, 2003 was scheduled to discuss the de-merger ratio recommended by the valuer was itself an unpublished price sensitive information as the agenda papers/notices given by DGL to the stock exchanges did not mention this.

4.10 By trading on the basis of unpublished price sensitive information, Shri Samir C Arora took an undue advantage and succeeded in avoiding losses to the tune of Rs. 23,56,59,637.06 (about Rs 23.57 crores) at the cost of buyers who had no such information. As per the practice prevalent in mutual fund industry, the incentives of the Fund Managers are linked to the performance of the funds managed by them. Thus being motivated by the personal gain that could accrue to him on account of performance incentive, he traded on the basis of said unpublished price sensitive information in the scrip of DGL.

- 4.11 Shri Samir C Arora was an “insider” in terms of the SEBI (Prohibition of Insider Trading) Regulations 1992. The evidence showed that Shri Samir C Arora had traded in the scrip of DGL when he was in possession of unpublished price sensitive information. Thus Shri Samir C Arora had violated Regulation 3 of SEBI (Prohibition of Insider Trading) Regulations 1992 and was therefore guilty of Insider Trading under Regulation 4 of SEBI (Prohibition of Insider Trading) Regulations 1992.
- 4.12 Shri Samir C Arora was managing the equity portfolio of ACMF and at the same time he was also managing the Indian allocation of FII/sub-accounts belonging to ACM. While doing so, he managed the portfolio of securities in the interest of sponsors and to the detriment of the unit-holders of ACMF, thereby he aided and abetted the violation of the above clause by the trustees and Asset Management Company of ACMF.
- 4.13 Clause 4 of Fifth Schedule of Code of Conduct states that Trustees and asset management companies must avoid conflicts of interest in managing the affairs of the schemes and keep the interest of all unit-holders paramount in all matters. In bidding for the stake of ACAML in collaboration with Henderson, Shri Samir C Arora had placed himself in a position of conflict of interest and thereby, he had aided and abetted the violation of Clause 4 by ACAML and ACAM Trust Co Ltd.
- 4.14 Shri Samir C Arora’s aforesaid conduct in aiding and abetting the Trustees and AMC of ACMF in violating the various provisions of SEBI (Mutual Funds) Regulations 1996, was detrimental to the interest of investors and the orderly development of the Securities Market.
- 4.15 In the aforesaid premises, Shri Samir C Arora was called upon to show cause as to why directions under Section 11(4) and 11B of SEBI Act, 1992, read with Regulation 11 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations 2003, Regulation 11 of SEBI

(Prohibition of Insider Trading) Regulations, 1992, Regulation 44 of SEBI (Substantial Acquisition of shares & Takeovers) Regulations, 1997 and Clause 1 and 4 of Fifth Schedule of the SEBI (Mutual Funds) Regulations, 1996 should not be issued against him.

- 4.16 An opportunity of inspection of documents referred to in the said show cause notice was granted to Shri Samir C Arora on 27.02.2004. Shri Samir C Arora filed his reply dated 09.03.2004 through his advocates. An opportunity of personal hearing was availed of by Shri Samir C Arora on 24.03.2004, when he attended the said hearing along with his counsel and made submissions broadly on the lines of his reply dated 09.03.2004.

Reply to Show Cause Notice and oral submissions

- 5.1 The submissions made on behalf of Shri Samir C Arora are summarized below:
- 5.2 News reports stating that Shri Arora was likely to resign from Alliance Capital if his joint bid with Henderson for the stake in ACAML was not successful were mere speculation made by the media without any basis or any input from Shri Arora.
- 5.3 ACAML has in its letter dated Sep. 10, 2003 to SEBI clarified that if Henderson's bid was not successful, Shri Arora would continue to work for Alliance Capital Singapore. It was made clear to all bidders, with the obvious exception of Henderson, that Shri Arora was an employee of Alliance Capital Singapore Office and hence, was not part of the sale of ACAML. It is clear that the person alleged to have been threatened (by Shri Arora) has clarified the factual position that Shri Arora was not a part of the stake sale proposal. It is therefore perverse to combine these circumstances and attribute to Shri Arora a malafide threat of resignation.
- 5.4 The show cause notice wrongly states that Shri Arora was the only fund manager for all the equity and balance funds of ACMF and was as for the Indian allocation

of various Asian Funds of Alliance Capital. Shri Arora was not managing all the off-shore funds of Alliance Capital. Besides Shri Arora, there were several other fund managers who were also managing various off-shore funds of Alliance Capital.

- 5.5 The fall in AUM of ACAML was due to rumours and speculation in the press and market uncertainty surrounding the potential sale. It is grossly erroneous to attribute such fall in the AUM to any action whatsoever on the part of Shri Arora, leave alone the allegation of his having held out a threat, with an intent to frustrate the sale process. Even if Shri Arora had been an employee of ACAML, it would have been his personal prerogative to resign his services whenever he chose.
- 5.6 Shri Arora was managing over USD 1 billion in equity assets in nine Asian Countries and the assets of ACMF were only about USD 250 mn. Shri Arora was based in Singapore and was being paid compensation commensurate with his responsibilities.
- 5.7 Shri Arora's compensation was being paid not by ACAML but by Alliance Capital Management (Singapore) Ltd. It was never envisaged by either Alliance Capital or Shri Arora himself that he would be working for any successful bidder (other than Henderson) after the completion of the sale. Alliance Capital informed all bidders that Shri Arora was not part of sale. The Information Memorandum of Blackstone group did not include Shri Arora's name in the list of key employees. If Shri Arora's services were part of the sale, then this document would have reflected the same. Since Shri Arora himself became a bidder along with Henderson, he did not participate in any presentation to various bidders.
- 5.8 All employees of ACAML based in India were offered a retention package to encourage them to stay with the firm until the sale was complete. Shri Arora and two other analysts based in Singapore were not offered this package as they were expected to continue working with Alliance Capital after the sale.

- 5.9 After the sale of the Indian business, Alliance Capital would no longer have been the sponsor of ACMF. ACAML would no longer have been the AMC of the fund. Since Shri Arora was an employee of Alliance Capital Singapore and not of ACAML and was not part of the sale, he could never have been the manager of the ACAML funds after the sale. Thus there was no ‘uncertainty’ regarding his continuance as a fund manager – in fact it was crystal clear to everybody that he would not be available after the sale.
- 5.10 The statement in the SCN citing media reports that Shri Arora had threatened to resign if his joint bid with Henderson was not successful was rendered false and inaccurate by the actual flow of events. When it was clear to Shri Arora and Henderson that the joint bid would not be successful, Shri Arora did not resign from Alliance Capital but continued to work.
- 5.11 Shri Arora initially opposed the plan to sell ACAML because of strong brand equity and shareholder value that had been created by ACMF. Once it became evident that sale would be pursued regardless of his objections and that a strong consortium could be formed with Henderson, Shri Arora notified his intent to participate in the bidding process. No further motive or connivance can be attributed to this development.
- 5.12 It is true that Henderson quoted a preliminary price range of USD 32 to 35m. However, it is perverse to link the same to the price quoted by HDFC as part of its pre-emptive bidding process in the week of January 13, 2003.
- 5.13 At the time of indicating the price range, Shri Arora’s consortium had no knowledge that a pre-emptive bid would be made and more so what such pre-emptive bid would be. The SCN is based on the fundamentally erroneous and unstated presumption that Shri Arora knew the pre-emptive price quoted by HDFC and then proceeded to destroy the AUM.

- 5.14 Shri Arora's and Henderson's original indicative bid amount was indeed higher than that of HDFC (no bid) and HSBC (USD 28.5 m) and still, Shri Arora and Henderson did not follow through with acquisition of ACAML.
- 5.15 Reduction in AUM in no way ensures that suddenly one bidder's price bid would become higher than HDFC. The fall in would impact all bidders uniformly.
- 5.16 SEBI has placed reliance on a purported set of facts unilaterally recorded by an officer of SEBI behind Shri Arora's back. Significantly, such officer is a person other than the designated Investigating Authority, and had no power to do so. It is important to note that such unilateral recording by an officer of SEBI is being passed off as a purported "statement" of Shri Arora. Such statement was not even shown to Shri Arora for his signature. This unilateral recording by the unauthorized officer came to light during the inspection before the post-decisional hearing. Based on such statement it has been repeatedly and wrongly pointed out that Shri Arora stood to gain personally from the bid along with Henderson. When such erroneous recording is rectified Shri Arora is accused of making contradictory statements. Further, to mitigate the apparent abuse of legal process, Shri Arora is now being accused of making false and misleading submissions to SEBI, which allegation too has been made by wrongly and selectively interpreting the MOU (between Shri Arora and Henderson).
- 5.17 The MOU between Shri Arora and Henderson was "only an expression of the (then) present intention" of Henderson and Shri Arora and did not "constitute a legally binding obligation or commitment". As per the MOU between Shri Arora and Henderson, the minimum equity for Shri Arora had been fixed at 16.67% of which the initial purchase would be of 6.67% with an additional entitlement of 10% of the equity. If Shri Arora left the fund voluntarily in the first 36 months, he would retain only 6.67% (which he would have paid for) and the additional 10% equity would be forfeited and transferred back to Henderson at no cost. It was

only if Shri Arora had stayed on with the fund for beyond 48 months that he could have retained the entire share holding.

- 5.18 Computation of the purported gain to be made (by Shri Arora) is without appreciating principles of valuation and the provisions of the MOU. The value of ACAML has been presumed to be USD 36 million. It has been forgotten that the pre-emptive bidder HDFC did not consider this to be right value, and the only actual bidder HSBC gave a price indication of USD 28.5 million. The selection of a value of USD 36m is therefore grossly arbitrary and unsubstantiated. This (10% additional equity) was meant to incentivise the continuance of Shri Arora with the fund for atleast 36 months. Even the additional 3.33% that would vest over 3 years was meant to be a deferred incentive for a continued stint with the fund. The shares to be received by Shri Arora (the additional principal equity and the vesting principal equity) could never have been sold by Shri Arora since they were not free and marketable. It is therefore incongruous and inappropriate to draw any reference in relation to managerial compensation and thereby attempt to quantify the extent of personal interest in the bidding process.
- 5.19 There is no evidence or record to suggest or demonstrate any calculated manner of creation of confusion and uncertainty. If Shri Arora had indeed acted in a calculated manner to create confusion, depress the AUM of ACMF, depress the bids of other bidders, then Shri Arora would have moved in to acquire ACAML after all bidders gave up. It is evident that this did not happen. Nor did he resign from Alliance Capital on the ground of the Henderson bid not succeeding.
- 5.20 From the recorded statement of Shri Johri dated September 5, 2003 it is apparent that he is being quoted out of context in the Show Cause Notice. In response to a query of SEBI regarding whether the Alliance Capital equity management style is peculiar, Shri Johri responded “This statement is a quote from a very well known TV commentator Shri Dharendra Kumar of Valule Research, New Delhi. He quoted this during his analysis with respect to the potential sale of the Indian

business by Alliance Capital. This statement was a often heard comment from market distributors and investors because many of them found the investment management style of the Portfolio Manager of Alliance Equity Funds very aggressive. Many distributors categorized Alliance Equity Fund in their analytical reports as aggressive. To that extent Shri Dhirendar Kumar was merely saying what was a common understanding of many market participants.” Shri Johri has also quoted Shri Dhirendra Kumar as advising viewers of CNBC “Investors were advised to watch for a confirmation re. the sale and then decide to redeem.” This also highlights that expert and respected market commentators like Shri Dhirendra Kumar were advising investors to switch out of Alliance Funds in case of confirmation of sale. Therefore redemption that happened in December and January cannot be attributed to actions/inactions of Shri Arora but to normal market response to a change in ownership and new management

- 5.21 In an e-mail sent to Shri Ajai Kaul on October 19, 2002, Shri Johri wrote (referring to the success of Alliance Frontline Equity Fund):- “.... this indicates the extent of the superiority of our equities franchise in India. No new buyer will be able to take this away with it and in the process we are about to begin, this will be destroyed day by day”. This clearly shows that even Shri Johri was very impressed with the equity franchise and the image and brand value that had been created for ACMF, and in being opposed to Alliance Capital’s intention to sell ACAML, he had noted with some dismay that no buyer could match this performance and maintain the same profile. In any event, it is unclear which penal provision of law is brought into play against Shri Arora by reason of Shri Johri referring to a journalist’s view on the purported aggressiveness of ACMF.
- 5.22 A fall in the assets under management is an inherent and conventional symptom of any proposed sale of a mutual fund business. It is universal experience for AUM to fall when there is proposed change of control over a mutual fund. Unit holders are always nervous about whether the funds hitherto being managed by a particular set of fund managers would continue to be handled in the same manner.

- During such times (of proposed change of control over a mutual fund) large, sophisticated and corporate investors, as a standard practice, withdraw their funds from debt mutual funds experiencing a change in control and move their resources to other mutual funds that do not have such circumstance around them.
- 5.23 The total sale of equity assets during the month of January 2003 was Rs.238.49 crores while the total sale of debts was Rs.713.33 crores. The redemption pressure was duly met by an orderly liquidation of investments made by the schemes in which the redemption had occurred. AUM in debt schemes fell 40% while AUM in equity schemes fell 24% - that the market was not reacting to Shri Arora's future, but to the fact that ACMF was experiencing a potential change in control. Had the redemptions and the fall in the AUM been due to Shri Arora, the emphasis of the fall would have been in the equity AUM and not in the debt AUM. There is no material correlation between the fall in the AUM of ACAML and fall in the NAV of the schemes of ACMF during the period in question (December 2002 – January 2003).
- 5.24 The NAV is arrived at by dividing the net assets of the scheme by the number of outstanding units of the scheme on the relevant valuation dated. Therefore, NAV is the value of one unit of a scheme. The NAV would fall as a result of a fall in the market price of securities held by the relevant scheme and not by the size of the resources that are being withdrawn from the scheme. Each of the sales of securities to pay for the redemptions witnessed during that period was met by the orderly liquidation of securities holdings at prevailing market prices.
- 5.25 Apart from Alliance Buy India Fund Scheme, every single equity fund of ACMF has outperformed the relevant benchmark index. In this regard it is pertinent to note that although BSE 200 has been referenced as the benchmark for the Alliance Buy India Fund, the scheme invested in consumer and healthcare sectors, and these sectors had under-performed the broader market that was reflected in the BSE 200. Despite significant redemptions in the schemes of ACMF, the

NAVs of the respective schemes of ACMF actually outperformed the relevant benchmark indices as well as comparable schemes of leading mutual funds in India.

- 5.26 Allegations in relation to losses being inflicted on the investors as a result of the significant redemptions in the schemes of ACMF are not sustainable since such allegations cannot be founded on mere conjecture and surmise. The NAV of Alliance New Millennium Fund (a technology-oriented fund) declined by 7.94% in the month of January 2003. During the same period the NAVs of other comparable technology-oriented funds declined by a higher percentage, such as the Franklin Infotech Fund which declined by 10.68% while Prudential ICICI Technology Fund declined by 12.35%; The NAV of Alliance Basic Industries Fund declined by 0.09% in the month of January 2003 while the NAV of Alliance Frontline Fund and Alliance Equity Fund declined by 2.42% and 4.34% respectively. During the same period, the NAV of comparable funds such as the Franklin India Blue Chip Fund declined by 2.49%, Birla Advantage Fund declined by 2.48% while Prudential ICICI Growth Fund declined by 5.35%
- 5.26 SEBI itself has envisaged a framework for exit by investors when there is a change in management in Regulation 22(e) of the MF Regulations, which inter alia provides that the unit-holders of a mutual fund have to be given the option to exit from the relevant scheme of the mutual fund at the prevailing NAV, without any exit load, in the event of a change in the controlling interest of the asset manager. Therefore, the redemptions ought not to raise any concern with SEBI.
- 5.28 In the case of Zurich India Mutual Fund (“Zurich MF”) there were reports sometime around November 2002 that the shareholders of the asset management company of Zurich MF were proposing to divest their shareholding in the asset management company. The AUM of Zurich MF which was at approximately Rs.4,500 crores immediately prior to the sales process having commenced, started declining and continue to decline till around March 2003 when the AUM reached

Rs.2685 crores. Only when it became certain that the HDFC Asset Management Company Limited was buying the stake of the shareholders of the asset management company to the Zurich MF, did the AUM of Zurich MF start increasing. The decline in the AUM of Zurich MF was approximately Rs.1815 crores, which was a percentage to the initial AUM of the Zurich MF immediately prior to the commencement of the sale process, is higher than the decline in the AUM of ACMF. More recently, just prior to the asset manager of the Principal Mutual Fund acquiring rights to manage the schemes of the Sun F&C Mutual Fund, the AUM of the Sun F&C Mutual Fund, which was approximately Rs.500 crores in May 2003, declined to approximately Rs.250 crores in November 2003. In percentage terms, the fall in the AUM of the Sun F&C Mutual Fund is also substantially higher than the fall in the AUM of ACMF.

- 5.29 The only consideration that SEBI, as a market regulatory and protector of investors' interests should have is the real impact on the small investor in the form of the movements in the NAV. A fall in the AUM can only impact the asset management company, which earns an ad valorem fee on the value of the AUM. As such, this issue is wholly irrelevant and is of no consequence to the small investor, whose interests; it is SEBI's duty to protect.
- 5.30 The manner of computation of the purported loss suffered by unit holders of the New Millennium Fund, the Buy India Fund, Alliance '95 and Alliance Equity Fund, proceeds on blatantly erroneous appreciation of NAV computation. The Show Cause Notice merely multiplies the number of units outstanding in January 31, 2003 by the difference between the NAV on that date and the NAV on December 2, 2002, to work out a purported aggregate value of loss. As stated earlier, the investors would have lost more had they invested in the benchmark indices. On the other hand, the erosion in the NAV is the function of various factors including market sentiment, investor perception of a proposed change in control, change in appetite for investment avenues, aversion to mutual funds that are on sale etc. Therefore, not only is the computation of purported loss

erroneous, but also attempting to fasten the liability for such fall in NAV on Shri Arora is baseless.

5.31 It is simply not apparent from the chain of events, even in the manner set out by SEBI in the SCN, that Shri Arora played any role at all in ‘thwarting’ the plan to sell ACAML to anyone but to himself and Henderson. The accusation relating to Shri Arora’s conduct, actions / inactions and his alleged ‘selfish motive’ are vague and incoherent. The SCN does not bring out how such charges can be linked to redemption of units of funds. So also, the redemption of units and the fall in NAV arising cannot form any basis of leveling allegations against Shri Arora. It is erroneous to suggest that there was any conflict between Shri Arora’s role as a fund manager and as bidder. In fact, Shri Arora was never part of the sale process and did have any interaction with the persons involved in the sale process. In fact it is not even SEBI’s allegation that there existed such an interaction. By such logic (conflict of interest between roles as fund manager and as bidder), every employee exercising a stock option would be in a position of conflict of interest between his role as an employee and his role as a person exercising a stock option. All forms of management buy out would have to be rendered illegal in India.

5.32 It is stated that ACMF and Alliance Capital along with the sub-accounts held significant quantity of share in (i.e. Digital Globalsoft Ltd., Balaji Telefilms Ltd., Mastek Ltd., Hinduja TMT Ltd. and United Phosphorous Ltd.) – It is stated that promoter holding is high in these stocks ranging from 33% to 58% as on December 31, 2002 and that there was low floating stock. The terms ‘significant holding’ and ‘low floating stock’ are vague and subjective terms. Suffice to say, that one ought to presume that these companies were compliance with the various provisions of securities laws that govern minimum public shareholding and promoter holding. All the allegations in relation to these stocks relating to the purported benefits being conferred on the offshore funds to the detriment of the domestic mutual fund, are leveled in hindsight, and in reality, at the time of

making the investments, no such thought process was even contemplated. Each fund has its own investment objectives as laid down by its respective charter and it was the duty of the fund manager to meet these objectives and deliver value to the unitholders and constituents. Shri Arora did not receive any differential compensation aimed at selectively helping the performance of the so-called sponsor/ FII funds.

- 5.33 On Sep. 5, 2001 the stock price (of BTL) closed at Rs.223.90 on NSE and at Rs.224.20 on BSE. On Sep. 11, 2001 the closing price on NSE was higher at Rs.226.55 while on BSE it was at Rs.226.70. On Sep. 6 & 11, 2001, ACMF and India Liberalization Fund (ILF) had together sold 6,35,300 shares. While the aggregate volumes on the two premier national exchanges (viz. BSE and NSE), where the price discovery takes place, was 73,71,592 shares. Even the cumulative sales on these two days, as a percentage of market volume, represented a miniscule 8.62% of volumes on these two days, which by no means be considered adequate to depress the market price. The contribution of the rest of the 92% of the market to the price discovery process cannot be wished away. Despite the sale, the actual price went up.
- 5.34 The purchases of 3,91,960 shares made on Sep. 19, 2001, were actually made on behalf of ACMF, and not Northern Trust Company (NTC) or any FII/sub-account, as implied in the SCN. Therefore, the first purchase after (the earlier) sale by ACMF was in fact made on behalf of ACMF itself and the beneficiaries were the Indian unitholders. ACMF purchased the shares first and NTC purchased it later (i.e on Sep. 26 & 27, 2001). Therefore, there is no question of benefiting the non-ACMF funds to the detriment of ACMF or ensuring any unfair advantage to the FII and sub-accounts. It is critical to note that despite the purchase of 3,91,962 shares at the price of Rs.186.42 per share (on Sep. 19, 2001), the price continued to fall further highlighting that the said transaction did not influence the price movements. Therefore, no allegation is sustainable.

- 5.35 Sale of 52,000 shares of HTMT during Jan. 16 to 29, 2003 were done to meet the redemption pressure. Once the pressure eased, the stock was once again included in the portfolio, which is why it was purchased again on Feb. 3, 2003. As a percentage of the volumes on the respective days, the sale by ACMF during Jan. 16 to 29, 2003 were far too miniscule to send any credible signal to the market – downward or upward. A sale of 52,000 shares can in no manner be considered powerful enough to have sent the price of HTMT into a downward spiral.
- 5.36 The sale on 1.75 lakhs shares of Mastek on Jul. 25, 2002 represented a miniscule 1.91% of the market volumes, and could not have impacted the price in any manner. On Jul, 29, 2002, ACMF purchased 1.00 lakhs shares of Mastek constituting 1.73% of volume traded on that day on both the stock exchanges (i.e. BSE and NSE). On Jul. 30, 2002, ACMF purchased another 1.00 lakhs shares of Mastek which was a mere 1.54% of volume traded on that day on both the stock exchanges while an additional 1.00 lakhs were purchased for the offshore funds. On Jul. 31, 2002, an additional 1.70 lakhs constituting a mere 1.13% of volume traded on that day were purchased for the offshore funds.
- 5.37 Although the scrip (of Mastek) was sold by ACMF at Rs.371.32 on Jul. 25, 2002, it closed on the NSE at Rs.373.60 and at Rs.369.35 on BSE – clearly higher than the previous close of Rs.355.75 and Rs.355.30 respectively. Thus, the sale on Jul. 25, 2002 had no impact whatsoever on the price – the stock in fact closed higher on that date. Therefore it cannot be alleged that the sale was made to depress the price or to hide the intention of increasing the holding at a lower price on a subsequent date. The price in fact moved up and profits were made, which it is the mandate and duty of a fund manager to ensure, in the best interests of the unit-holders.
- 5.38 On Jul. 29, 2002, ACMF has purchased 1 lakh shares of Mastek at Rs.355/- since the price had fallen (well after the sale on Jul. 25, 2002) – on that date the stock closed at Rs.362.95 on NSE and Rs.362 on BSE. On Jul. 30, 2002, ACMF and

off-shore funds had together purchased 2.0 lakhs shares of Mastek at a price of Rs.357-358/. On that date, the stock closed at Rs.352.35 on NSE and Rs.348.65 on BSE. On Jul. 31, 2002, an additional 1.70 lakhs shares of Mastek were purchased at Rs.323 for the offshore funds. On that date, the stock closed at Rs.349.85 on the NSE and Rs.354.25 on the BSE.

- 5.39 That the price does not react to the purchases made by Shri Arora is further evidenced from the fact that despite purchases between Jul. 29 and 30, 2002, the price continued to fall. This demonstrates that the sales or purchases effected by Shri Arora did not have a corresponding impact on the price. In fact, the price moved upwards when he sold and moved down when he purchased. – clearly rendering the charge of moving the price upwards or downwards, baseless.
- 5.40 ACMF and off shore funds had together purchased 4.00 lakhs shares of Mastek on Aug. 23, 2002. Subsequently, the price of the scrip rallied and they together sold 2.50 lakhs shares.
- 5.41 There is nothing in the securities laws that prevents a sale in a day when a purchase is made earlier in the day. It is incumbent on a fund manager to maximize profits for unit holders and constituents. Therefore, it is erroneous to allege that the offshore funds were benefited by Shri Arora, particularly, when it is seen that ACMF made Rs.63 lakhs on that date as compared with Rs.19 lakhs earned by the offshore funds on that date. On Oct. 1, 2002, ACMF (3.10 lakh shares) and the off-shore funds (1.50 lakh shares) had together sold 4.60 lakhs shares of Mastek at Rs. 397/- and Rs.396/- respectively. On Oct. 3, 2002 ACMF had sold another 1.85 lakhs shares of Mastek at an average of Rs.381/-, “the price had fallen since the last sale”.
- 5.42 On Oct. 4, 2002 based on the research input of Shri Bhaskar Laxminarayan, it was decided to increase the weightage of certain software companies including Mastek, Digital and Infosys. Accordingly, ACMF bought back 5.70 lakhs shares

of Mastek and the off shore funds 1.00 lakhs shares on the same date at prices of Rs.388-389/-. Therefore no allegation of creation of artificial trading volume is sustainable.

5.43 SEBI is aware, both mutual funds and FIIs can trade only on a delivery basis and have to deliver or take delivery of every single sale and purchase made by them. Against this context, there is no scope for levelling any charge of creation of artificial volumes in any stock.

5.44 The volumes have always been huge in this stock (i.e. Mastek). The contribution to the volumes by the impugned transactions (i.e. on Jul. 25, 29, 30 and 31, 2002, August 20, 22 & 23, 2002, Oct. 1, 3 & 4, 2002) is far too minor. Therefore, the allegation relating to purported creation of artificial volumes simply cannot be levelled – even considering the facts set out in the SCN itself.

5.45 The sale of UPL shares during December 2002 to January 2003 were aimed at meeting the redemption pressure and was part of the orderly liquidation of assets in schemes where there were redemption requests. There was indeed no impact on the price owing to these sales and the percentage sale to the total volumes were quite small. Between Oct. 1 & 18, 2002, the price of UPL steadily moved up from Rs.153.25 to Rs.168.75. On Oct. 10, 2002 itself despite ACMF and FII net selling of 1.74 lakhs, UPL's price closed at Rs.175.40 on NSE and Rs.173.10 on BSE – higher in both the cases than the prices on the previous day. This clearly demonstrates that ACMF and ACM were in no position to influence prices even for a day and that their selling or buying did not have any adverse impact on the prices. Therefore, it is blatantly erroneous to suggest that the sale by ACMF was motivated only to depress the price and create room for ILF to purchase the shares.

5.46 Shri Arora cannot be alleged to be benefiting Alliance Capital and its off-shore affiliates at the same time as the allegation of his threatening to quit Alliance Capital and thereby thwart the process of sale of ACAML.

- 5.47 With regard to the interview to Business Standard dated May 5, 2003, regarding the prospects of DGL, there is nothing in the SCN to indicate any allegation about which part of the statement is misleading in any material particular. To fit within the ambit of Regulations 5 of FUTP Regulations, a statement has to be materially misleading and the statement ought to be likely to induce a transaction in securities. In the absence of anything misleading, Regulations 5 of FUTP Regulations has no application to the facts of the case.
- 5.48 The statement merely points out that a merger of DGL with HPISO was likely. It was not hard to guess, because the worldwide merger of HP and Compaq had been announced. The obvious benefits that such a merger would have for Digital was set out in the said statement, and therefore there was nothing misleading in the said statement. Even if such a statement could be considered to be misleading merely because ACMF sold its holdings in DGL on May 8, 2003 – eight days after the interview – such statement clearly falls within the ambit of a general comment akin to a comment on trends in the securities market or on the economy.
- 5.49 The entire burden of allegations pertaining to alleged violation of Takeover Code is completely erroneous and baseless. These allegations proceed on the premise that ACMF, Alliance Capital and its FIIs and sub-accounts are all persons acting in concert. There is no elaboration or consideration of facts as to whether these various pools of resources could be considered to be acting in concert.
- 5.50 Even assuming for the sake of argument that these funds were all acting in concert, the notice does not even deal with the submissions made by Shri Arora that the burden of filing reports under the Takeover Code rests solely with the compliance officer than with the fund managers. In fact, the MF regulations made it clear that the compliance officer ought to report directly to the Trustees of the mutual fund and not to the fund manager or the chief executive officer of the AMC. Several disclosures were indeed made by each of the entities concerned

under the requirements that were specifically applicable to each of them. SEBI's charge is that these entities did not aggregate their holding for the purpose of disclosure, and proceeds to hold Shri Arora responsible for the same. In no mutual fund is the fund manager responsible for computing the overall holding in any listed company across various schemes and funds managed by him. Since reporting requirements under any provisions of securities law is not the fund manager's responsibility, there is simply no basis whatsoever for leveling such a serious technical compliance-related allegation against Shri Arora.

5.51 Whether or not two or more persons are acting in concert is always a mixed question of fact and law to be determined from the facts and circumstances of the case. Even where a deemed action in concert is presumed in law, the presumption is rebuttable and facts have to be examined to consider whether the contrary is likely to be established. The SCN does not even attempt to demonstrate that these persons are acting in concert. Two or more persons can be said to be acting in concert only if they have a common objective or purpose of substantial acquisition of shares or voting rights or gaining control over a target company pursuant to an agreement or understanding, or they co-operate in such acquisition. There has to be an animus and a conscious effort and agreement and understanding with a common objective of acquisition. Each of the funds has a different investment objective in their respective charters.

5.52 It is SEBI's own case that there were several instances where ACMF was selling but FIIs and sub-accounts were buying and vice versa. Against such backdrop, it cannot be argued by SEBI that there was any action in concert between ACMF and the other funds. When ACMF was purchasing the other funds such as ILF and ATF were selling and vice versa. When one was a net purchaser, the other was a net seller. This too clearly demonstrates that there was not common objective or purpose in the acquisitions.

- 5.53 The concept of acting in concert has no application to Regulations 13(3) of Insider Trading Regulations. Under the Insider Trading Regulations every acquirer has to make a disclosure.
- 5.54 The scheme and perspective behind the Insider Trading Regulations is very different from the scheme of the Takeover code. The Takeover code regulates substantial acquisition of shares and / or control while the Insider Trading Regulations regulate and prohibit trading on the basis of insider information. Even assuming that allegations can even be considered under the Insider Trading Regulations, no charge of non-disclosure can be leveled under any provision of Regulations 13 of Insider Trading Regulations
- 5.55 The allegation that Shri Arora being aware of the combined holding of ACMF and the PACs, failed to advise ACMF about the holdings of the other funds is blatantly unsupported by evidence and material on record. There is no material basis to suggest that Shri Arora was trading without the custodian or the back office being aware of his trades. Therefore such a charge ought to fail and cannot be levelled.
- 5.56 As per the internal notings of various officials of SEBI regarding the definition of 'persons acting in concert' FII with sub accounts cannot be deemed to be acting in concert with mutual fund along with AMC/ sponsor/ trustee even if FII and mutual fund are under the same parent group. Therefore, in our opinion there is no violation of the takeover code in letter and spirit.
- 5.57 SEBI's communication to ACAML stated that "It is clarified that your practice of excluding FII/sub-accounts of your parent organisation while aggregating the holding across all schemes with holdings of the Trustee Co. and AMC for ascertaining the 5% limit under the Takeover Code is in order".

- 5.58 Shri Arora was not even an employee of ACAML and therefore, there was indeed a Chinese Wall between the compliance function and Shri Arora's fund management operations.
- 5.59 There is no basis for alleging that Shri Arora's conduct was detrimental to the interests of the investors and the orderly development of the securities market, enabling SEBI to issue directions under Sections 11(4) and 11B of the Act. It is in fact true that such directions have already been issued for ever seven months now, and in hindsight, post facto reasons are being searched for to justify the action already taken.
- 5.60 Merely on the basis of sequential recording of facts, the Show Cause Notice concludes that the sale of 66,140 shares (of Digital Global) in four consecutive trading days since May 6, 2003 amounts to sale on the basis of price sensitive information.
- 5.61 SEBI has inferred that the market perceived the ratio report as being unfavourable to Digital Shareholders since the price of Digital fell from Rs.500.5 (closing price as on June 6, 2003) to Rs.371.1 on June 9, 2003.
- 5.62 Shri Arora's interview with CNBC on an undated day in June 2003 has been extracted. The extracts merely suggest that the market these days, seeks an explanation for how such ratios are compared, and that ratio was unfair.
- 5.63 The relevance of the fact that "There were no transactions in Digital by the funds under Shri Arora's management since April 11, 2003" is not made clear.
- 5.64 No explanation has been provided about whether SEBI considers the sealed envelope to have been opened.

- 5.65 The reference to “Event risk from tomorrow’s announcement” in the explanation for the sale recorded on May 9, 2003 was “supposedly” a reference to the merger ratio. The ratio was not announced the next day – it was announced a month later from San Francisco. The announcement that was actually made the day after May 9, 2003 was the financial results for the quarter ending March 2003, but this has not been explained (in the SCN of SEBI).
- 5.66 The agenda papers for May 12, 2003 board meeting did not have any mention of a discussion of the ratio report. This only goes to show that the reference to “tomorrow’s announcement” was a reference to the financial results and other matters such as whether or not there would be a merger, integration timetable and such other uncertainties. When a merger is talked about widely in the public domain, the convening of a board meeting itself leads to speculation and uncertainty – the market does not look for the agenda list. Moreover, this board meeting was a few weeks leading to uncertainty.
- 5.67 There was a hurry to dispose of the ACMF holding by May 12, 2003 since an agenda item for the board meeting was “Integration Related Items” This is contradictory to the earlier criteria (of SEBI). If Shri Arora had inside information, he would have known that the ratio would not be disclosed on that date and there would be no urgency to complete the sale before May 12, 2003.
- 5.68 Shri Som Mittal knew Shri Arora for five-six years. The fact that Shri Mittal never met or communicated with Shri Arora throughout 2003 is simply ignored. In a statement of Shri NVP Tendulkar, Chief Finance Officer & Company Secretary, Digital recorded on August 20, 2003, it has been expressly stated that the last interaction between Digital and Shri Arora was in an analyst conference in April 2002, and that no fund manager or analyst from Alliance Capital had visited Digital throughout 2003. SEBI has ignored the statement.

- 5.69 Shri Arora and his analysts made regular visits and interacted with management and senior officials of companies in which they invest, and discussed performance. This is the stated investment strategy of several mutual funds including those that are internationally reputed and highly regulated. Such meetings alone do not prove the sharing of unpublished price sensitive information; these meetings aid the appreciation of information that is already in the public domain.
- 5.70 ACM had a special interest in Digital since the funds' holdings in Digital represented the single largest holding after those of Compaq. How the fact of being second largest shareholder (itself not proven) can lead to a presumption of having access to unpublished price sensitive information is not explained.
- 5.71 If anybody could compute the merger ratio, how would it be price-sensitive? Moreover, BSM's statement that one could not have computed the ratio unless one knew of HP's financials has not been dealt with.
- 5.72 SEBI has recorded that Shri Hemant Soonawala carried the sealed cloth envelope and admittedly, there is no allegation of any interface between Shri Soonawala and Shri Arora from the record.
- 5.73 The SCN (of SEBI) has twisted the interpretation of the term 'person deemed to be connected person' under Regulations 2(h) of Insider Trading Regulations to suggest that any market intermediary could be a person connected with any other person in India.
- 5.74 Shri Arora is not an intermediary in the capital market registered with SEBI under Section 12 of the Act, and was not providing any service to Digital in order to be deemed to be connected with Digital. Shri Arora was not even an employee of ACAML for him to fall within the charge of Regulations 2(h) of the Insider Trading Regulations

- 5.75 The SCN does not deal with how Shri Arora is purported to have come in possession of the allegedly price-sensitive information. The SCN does not even credibly accuse any insider of having shared unpublished price sensitive information with Shri Arora.
- 5.76 The SCN does not show how Shri Arora could be considered to be an ‘insider’ within the meaning of the term as defined in Regulations 2(e) of Insider Trading Regulations. Even if one were to assume that SEBI would consider Shri Arora to be a ‘connected person’ within the meaning of the term in Regulations 2(c) of the Regulations, the onus is on SEBI to demonstrate the connection.
- 5.77 The reference made by SEBI to Regulations 2(h) is of no use since it only provides for Shri Arora being an insider to the mutual fund that he worked for.
- 5.78 It is only against Shri Arora that SEBI has taken action in the form of directions under Sections 11(4) and 11 B of the Act – there is no whisper of any proceedings in respect of BSM, any members of the board of directors of Digital or even the sub-committee of independent directors or the senior management of Digital.
- 5.79 Unless it is demonstrated that a person was actually in possession of unpublished price sensitive information. In the absence of any cogent or coherent evidence, whether direct or circumstantial, the SCN has been unable to show how Shri Arora allegedly came in possession of the purported unpublished price sensitive information. Owing to the failure to demonstrate that Shri Arora was indeed in possession of unpublished price sensitive information, the SCN fails to make a sustainable charge of Shri Arora’s transactions being in violation of Regulations 3 of Insider Trading Regulations unless SEBI is able to successfully invoke the provisions of Regulations 3 of the Insider Trading Regulations, the provisions of Regulations 4 are of no consequence.

- 5.80 SEBI has not brought any material on record to question the credibility of the denial of interaction between Shri Som Mittal and Shri Tendulkar of Digital with Shri Arora. The possible motivation that Shri Bansi Mehta, Shri Som Mittal or any other person could have had, to share adverse inside information with an institutional investor that had sold more than 17,00,000 shares in the past six months, has not been dealt with. In view of the same, the sweeping assumption that Shri Arora was in possession of price sensitive information falls within the realm of conjecture, and no penal provision can be invoked in such circumstances.
- 5.81 The reason for the sale of Digital was that the stock was downgraded to a ‘SELL’ recommendation by CLSA Emerging Markets’ research analyst M/s Aniruddha Dange and Bhavtosh Vajpayee vide their report published on May 8, 2003. CLSA Emerging Markets was voted as India’s No.1 FII broker. Shri Dange was voted as India’s top equity analyst by Asiamoney, and his downgrade carries immense credibility in the market. In fact, SEBI’s belief that there was nothing adverse about Digital during the period from May 8<sup>th</sup> to May 12<sup>th</sup> to prompt selling of DGL is untenable in view of the CLSA research report itself. The reason for the continued selling after May 8, 2003 was that Shri Bhaskar Lakshminarayan, the internal analyst working with Alliance Singapore had downgraded the stock to “2” and strongly recommended reducing the position in the stock.
- 5.82 These responses from Shri Arora set out in his written submissions dated Aug. 27, 2003 have not been dealt with in the SCN (of SEBI).
- 5.83 A person who is accused of Insider Trading would never transparently write in his reasoning that he was relying on unpublished price sensitive information to sell. It beats all expectations of a prudent person to record in writing the very fact of intention to commit Insider Trading as a reason for the sale.
- 5.84 By some convoluted logic, it has been alleged that Shri Arora stood to gain by his performance-linked bonus from the timely sale of Digital, which purportedly

saved ACMF a loss of Rs.23.57 crores. This allegation does not link with the conduct of Shri Arora, since he proceeded to resign from Alliance Singapore in August 2003. Had he indulged in Insider Trading to reap the benefits through the bonus, he would have waited another four months to bag his bonus and then resign from his job.

5.85 It is surprising to note that SEBI has found it fit to impose a penalty in the nature of an order under Sections 11(4) and 11B of the Act against an individual fund manager of a mutual fund even while invoking provisions of the Code of Conduct that govern the mutual fund itself. The code of conduct is cross reference to Reg, 18(22), 25(16) and 68(h) of the MF Regulations. Regulations 18(22) casts an obligation on the trustees of a mutual fund to observe the code of conduct while Ref. 25(16) casts a similar obligation on the AMC. Regulations 68(h) of MF Regulations renders a mutual fund liable for enquiry proceedings for code of conduct. Nowhere in any of these charging provisions is there any liability or obligation imposed on any individual fund manager who may be employed by a mutual fund.

5.86 Although the allegation is one of aiding and abetting the violation of clause 4 by ACAML and ACAM Trust Company Ltd., the SCN entirely blames only Shri Arora in relation to the bid along with Henderson. It follows by reason that all the allegations and false inferences drawn ought to be withdrawn by SEBI.

## **CONSIDERATION OF ISSUES**

6.1 Keeping in view interim orders dated August 9, 2003 and September 24, 2003, I have carefully considered the findings of the investigation communicated in the show cause notice dated February 20, 2004, the reply to the show-cause notice vide letter dated 9<sup>th</sup> March, 2004, material on record as inspected by Shri Samir C. Arora, and the oral submissions made on behalf of Shri Samir C. Arora by his

advocates during the hearing held on March 24, 2004. The following issues arise for consideration.

- Whether Shri Samir C Arora is guilty of professional misconduct inviting action under Section 11(4) and 11B of SEBI Act, 1992?
- Whether Shri Samir C Arora is guilty of violating the provisions of Regulations 4(a), 4(b), 4(c), 4(d) and 5 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995?
- Whether Shri Samir C Arora is guilty of violating the provisions of Regulation 3 of SEBI (Prohibition of Insider Trading) Regulations 1992 ?

6.2 For the sake of clarity, while dealing with the issues, I propose to consider the submissions/ arguments of Shri Arora with reference to the allegations, in a logical sequence as under:

#### First Issue

Whether Shri Samir C Arora is guilty of professional misconduct inviting action under Section 11(4) and 11B of SEBI Act 1992?

7.1 At the outset, the basic contention of Shri Arora that he was not an employee of ACAML, needs to be dealt with. This issue had been examined in my earlier interim order. The following facts are relevant for consideration:

- Key Information Memorandum and Common Application Form (a publicly available document) of ACMF under the Title ‘Asset Management Company’ listed Shri Samir C. Arora as one of the principal officers of the ACAML. It also states Shri. Samir C. Arora as the fund manager for various schemes of ACMF.

- The Confidential Information Memorandum of ACAML dated November 2002 prepared by the Blackstone group contained (as submitted by Shri Samir C Arora in his reply) under 'Management and Employees' the organization chart of ACAML listed Shri Samir C. Arora, Sr. Vice President Head - Asia Emerging Markets reporting to the ACAML board.
- Press release dated February 3, 2003 issued by Alliance Capital states "Samir Arora will continue to act as Chief Investment Officer of Alliance Capital's Indian operations....." Commenting on the occasion, Shri Samir C. Arora stated "I am pleased to continue my deep involvement in the Indian markets as Portfolio Manager for Alliance Capital's Indian equity investments".
- Shri Samir C. Arora has on June 20, 2003 stated under oath that he is the portfolio manager for all the equity funds of ACAML.
- ACAML has also submitted that Shri Samir C. Arora, a key personnel of ACAML is its Chief Investment Officer and Fund Manager for Equity and Balanced Funds.
- Shri Samir C. Arora in his written submissions has himself submitted that he "is responsible only for the equity fund management operations of ACMF", his "role was purely that of Fund Manager".

7.2 From the aforesaid facts it is clear that Shri Samir C. Arora was one of the key personnel of ACAML and in his capacity as fund manager he was managing the equity and equity portion of balanced schemes of ACMF. Further, the aforesaid status of Shri Samir C. Arora was also disclosed to the unit-holders at large through Key Information Memorandum and Common Application Form. It is also observed from the organizational structure of ACAML as given in Confidential Information Memorandum, November 2002 (which was given to the prospective

bidders) as submitted by Shri Samir C. Arora I find that Shri Samir C. Arora was reporting to ACAML board.

- 7.3 Hon'ble Supreme Court in the case of Chintaman Rao vs. State of M.P. AIR 1958 SC 388 has, inter-alia, stated that the concept of employment involves three ingredients: (1) employer (2) employee and (3) the contract of employment. The employer is one who employs i.e. one who engages the services of other persons. The employee is one who works for another for hire. The employment is a contract of service between the employer and the employee whereunder the employee agrees to serve the employer subject to his control and supervision.
- 7.4 Further, as per Black's Law Dictionary, Employee means 'A person who works in the service of another person (the employer) under an express or implied contract of hire under which the employer has the right to control the details of work performance.'
- 7.5 In Multinational corporate practice, it is not uncommon that one person provide services to more than one company belonging to the same group situated in different countries.
- 7.6 I find that ACAM Trust Company Pvt. Ltd., the Trustee Company of ACMF has stated that "It is the global practice at Alliance Capital that employees are paid their salaries by their relevant Alliance Capital subsidiary/affiliate, in the country in which such employees are located. However, Alliance Capital employees may continue to act as officers of the various Alliance Capital subsidiaries/affiliates around the world for which they have been allocated responsibilities as necessary and appropriate."

In view of the aforesaid facts I do not find any merit in Shri Samir C Arora's submissions that he was not an employee of ACAML.

- 7.7 I note that it was the general perception that Alliance Mutual Fund and Shri Samir C. Arora were almost synonymous. I also note that he was known for his aggressive style of functioning. He had gone on record confirming his deep involvement in Indian market as portfolio manager in equity investment. It is also observed that when Shri Arora learnt that Alliance Capital intended to sell off its Indian business, Shri Arora and other senior managers in India urged Alliance not to exit the Indian market. It has not been denied that having failed in his efforts to persuade Alliance from selling ACAML, Shri Arora joined hands with Henderson and submitted a bid. It is also observed that Henderson's bid for ACAML was less than that of HDFC. It is noted that HDFC initially quoted in the range of USD 42 to 50 million as against the initial bid of Henderson at USD 30 to 33 million.
- 7.8 It is clear from the MOU between Shri Arora and Henderson that Shri Arora did stand to gain personally from his joint bid with Henderson. As per the MOU Shri Arora was entitled to buy stake of 6.67% and to receive 10% additional equity free of cost. In addition, he was to receive 3.33% vesting Principal equity which will vest in equal portions over three years. In his earlier written submissions dated August 27, 2003 to SEBI (page 18 para 19) as well as in the submissions to SAT Shri Arora had contended that "for continued performance and loyalty to the mutual fund over the next four years, the Respondent (i.e Shri Arora) was to receive 13.33% shares, in the form of sweat equity." Thus, the earlier submissions by Shri Arora to SEBI (and SAT) were indeed misleading.
- 7.9 I find that while, on the one hand, Shri Arora is contending that reliance should be placed on the MOU to ascertain whether Shri Arora stood to make any personal gain, he is attempting, on the other hand, to play down the sanctity of the MOU between himself and Henderson, by trivializing it only as an 'expression of the intentions' of the parties and not a legally binding document. In any case, what is pertinent here is the intentions of the parties concerned, which is clearly reflected in the MOU.

- 7.10 From the terms of the MOU it is clear that Shri Arora would be richer by 10% additional principal equity (which he would have received free of cost) if his bid along with Henderson was successful. He is attempting, however, to play down the significance of the likely personal gain by citing the eventualities that may deny him the benefit. It is clear that while entering into understanding with Henderson, Shri Arora had every intention to acquire the fund and continue with the fund once his bid along with Henderson was successful.
- 7.11 Further, I find that certain terms of MOU ensured that his personal gain would be much more than the 10% additional principal equity which he was, in any case, entitled to free of cost e.g. “Should the investor (i.e. Henderson) exit prior to the vesting of these options (i.e. the 3.33% vesting principal equity) and the Principal (i.e. Shri Arora) also exits his entire stake at this time, the unvested portion will vest immediately. As a further incentive to the Principal (i.e. Shri Arora), the Principal will have the right to acquire up to an additional 5% of the equity in Alliance India over the next four years (This 5% can be acquired in part or whole). The purchase price will be at a price which provides the Investor with an IRR of 20%.”
- 7.12 Thus, it is seen that the terms of the MOU, while casting certain obligations upon Shri Arora, had clauses which would have led to his tremendous personal gain if he continued with the fund (after winning the bid) and as discussed in the para above, he had every intention to continue with the fund if his bid was successful. Reckoning the value of ACAML at USD 36 million, Shri Arora was to receive about Rs.16.50 crores (reckoning Rs.46/USD). Thus, Shri Arora would have made an initial personal gain of Rs.16.50 crores and an additional Rs.5.50 crores (being the value of vesting principal equity of 3.33%).
- 7.13 Shri Arora is arguing that USD 36 million is not the right value for ACAML as a base for the calculation of the benefit that would accrue to him, I find that Shri Arora himself had indicated a price of USD 32-35 million in his revised bid

for ACAML. When the bidding was in progress, Alliance Capital had demanded a minimum price of USD 36 million for its stake in ACAML. Thus, while one may quibble over the then value of ACAML (which in any case can only be an estimate), the value of USD 36 million appears to be a reasonable estimate for computing the potential personal gain of Shri Arora. Thus there is no denying the fact that Shri Arora stood to make substantial personal gain if his bid with Henderson was successful. I do not agree with the contention that the shares to be vested in his favour could never have been sold. If the shares to be vested are never encashable it would negate the very purpose of the entitlement.

- 7.14 I find that SCN of SEBI merely narrates the information obtained by SEBI from Alliance Capital and does not in any way indicate that SEBI has accepted that mere rumours and speculation in the market and market uncertainty surrounding the potential sale led to the fall in AUM. Shri Arora is trying to twist the narration of information in the SCN and twist it as SEBI's conclusion that he was not responsible in any manner to the fall in AUM of ACAML.
- 7.15 It is clear that the fall in AUM of ACAML was not merely due to rumours and speculation regarding the proposed sale, but due to the uncertainty regarding the continuation of Shri Arora as fund manager. While Shri Arora let the rumours persist without clarifying the matter to the public his team members added to the confusion and uncertainty by proposing to quit the fund if it was not sold to Shri Arora and Henderson. The persistent rumours about Shri Arora leaving the Fund and redemption pressures should have normally edged anyone in Shri Arora's place to clarify the matter to the public, so as to stem the redemption pressure. The fact that he did not choose to do so, corroborates the doubt that he did deliberately induce the redemption pressure and thus fall in AUM of the fund, to gain a bargaining power as bidder.
- 7.16 It is true that Shri Arora, like any other employee, has a right to resign; In fact he had an ethical obligation to resign, to avoid conflict of interest; but Shri Arora did

not do so. Instead, he did not make any efforts to deny the rumours and speculations about the impending exit of himself and his team or to clarify his position to the unit-holders whose interests he claims to uphold.

- 7.17 I find that the unit-holders of ACMF were kept in dark regarding the role of Shri Arora in the proposed stake sale. This caused confusion and uncertainty in the minds of unit-holders regarding the continuation of Shri Arora with the mutual fund.
- 7.18 On perusal of the Confidential Information Memorandum dated November 2002, of the Blackstone Group it is observed that Shri Samir C Arora's name figured in the organizational chart of ACAML under the heading Management and Employees. There is no express clause in the Confidential Information Memorandum indicating that he was not part of the business that they were intending to purchase. Therefore, there is no merit in the contention that all the bidders were fully aware that Shri Samir C. Arora was not part of the business that they were intending to purchase.
- 7.19 In support of his claim that he was not part of the sale of the Fund, Shri Arora has contended that all key employees of ACAML other than himself met and made presentations to the various bidders. Obviously, this team of ACAML included the two analysts who were employees of ACAML (and belonging to Shri Arora's team and who had indicated their unwillingness to continue with the fund if it was sold to any bidder other than Shri Arora and Henderson). Non-participation in the presentation need not necessarily mean not being a part of the sale. Shri Arora in his submission dated August 27, 2003 to SEBI, has informed that Shri John Carifa, the then chairman of Alliance Capital offered 2% of gross proceeds received by Alliance Capital as incentive for assisting smooth transition of assets to HDFC. While the present contention of Shri Arora that no package was offered by Alliance Capital to him in connection with the proposed stake sale contradicts

his earlier stand, the purpose of providing incentive to Shri Arora appears to be a price for his co-operation.

7.20 Whether the issue of continuance of Shri Arora as fund manager of ACMF post-sale was known to the prospective bidders is itself a moot point. In such a scenario, by no stretch of imagination can it be said that the issue was crystal clear to everybody including the unit-holders of ACMF whose interests should have been the paramount consideration of Shri Arora. No inference can be drawn from the fact that Shri Arora did not actually resign from Alliance Capital since the Alliance Capital had abandoned the proposed stake sale, which, in any case, he was opposed to and Shri Arora continued to work in his earlier position. I find that Shri Arora has not denied the media reports attributed to him that he threatened to resign if his joint bid with Henderson was not successful. The above contention confirms the narration of events as contained in SEBI's SCN dated February 20, 2004.

7.21 It may be noted that, Shri Arora's consortium could not have foreseen a pre-emptive bid from some one, at the time of submission of their bid. However, once HDFC made the pre-emptive bid, Shri Arora did come to know about the pre-emptive price quoted by HDFC. The same is clear from Alliance Capital's response to SEBI (as furnished in para 4.1 of SCN) that Alliance Capital advised the other bidders (obviously including the Arora- Henderson combine) regarding the pre-emptive bid. Shri Arora himself, in his submission to SEBI dated August 27, 2003 has mentioned (at point 10 page 14) that the correct facts / sequence of events to the stake sale proposal was in the week of Jan. 13, 2003 "HDFC Mutual Fund is believed to have made a pre-emptive bid stating that it was willing to close the deal to acquire ACMF immediately, if the transaction price was close to some specific fixed amount. It was reported that the amount offered was US\$ 36 million." Thus, I find that the present denial of Shri Arora that he had no knowledge of the pre-emptive price quoted by HDFC is not tenable. That Shri Arora knew the pre-emptive price quoted by HDFC, when the process of

bidding was in progress is a fact. It is neither a presumption nor is it erroneous as is being dubbed by Shri Arora.

- 7.22 The sequence of events during the proposed stake sale shows that only HDFC revised their bid in response to the fall in AUM. Apparently there was no downward revision in the bid by Shri Arora and Henderson, in response to the falling AUM. In fact, the only revision in the bid of Shri Arora and Henderson was upwards i.e. from USD 30-33 million to USD 32-35 million. Hence, the contention of Shri Arora that any fall in AUM will impact all bidders uniformly is not in consonance with his own actions.
- 7.23 It is clear from the above that Shri Arora did let the rumours and speculations regarding his and his team's impending exit to persist as the uncertainty created by such rumours and speculations were to his advantage.
- 7.24 It is clear that the bid of Shri Arora – Henderson combine was USD 32 – 35 million while the minimum amount sought by Alliance Capital was USD 36 million. Due to the significant difference in the bid amount of Shri Arora – Henderson combine and that sought by Alliance Capital, the bid of Shri Arora – Henderson combine was not successful.
- 7.25 Shri Samir C Arora contended that the statement dated 05.09.2003 of Shri Nikhil Johri, former CEO of ACAML, was quoted out of context in the showcause notice. I do not find any merit in the said contention. Shri Arora himself has in his reply relied on the said statement of Shri Johri and that of Shri Dharendra Kumar (as quoted by Shri Johri) to state that the redemption that happened in December and January cannot be attributed to actions/inactions of Shri Arora but to normal market response to a change in ownership and new management. I note that Shri Arora has also not disputed the veracity of the statements of Shri Johri and Shri Dharendra Kumar.

- 7.26 It is clear from the statement of Shri Johri and Shri Dharendra Kumar that Shri Dharendra Kumar was advising the investors of ACMF to switch out of Alliance Funds due to the uncertainty regarding the continuance of the portfolio manager of Alliance Equity Funds (i.e. Shri Arora) and not due to the likely change in ownership of ACAML as alleged by Shri Arora.
- 7.27 The views expressed by Shri Johri refer to the aggressiveness of the portfolio manager of Alliance Equity Funds (i.e. Shri Arora) as perceived by the market participants. Though no penal provision of law is attracted by the above statements of Shri Johri, the statement of Shri Johri further confirms the significance of Shri Arora's role in ACMF as perceived by the market. This shows that the contention of SEBI that the significant redemptions faced by ACMF during the proposed stake sale was due to the uncertainty regarding the continuance of the portfolio manager of equity funds (i.e. Shri Arora) and not due to the proposed change in ownership, is not without basis.
- 7.28 According to Shri Arora "it is a universal experience for AUM to fall when there is a proposed change of control over a mutual fund." The universal truth, however, is that redemption pressure would depend on the perception about the impending new management. Shri Arora has in his reply rightly observed that the uncertainty regarding the continuance of the fund managers causes nervousness for unit holders. In the case of ACMF, Shri Arora was the sole fund manager for all the equity schemes of ACMF. Thus it is clear that the unbridled uncertainty of the continuance of Shri Arora was bound to play a significant role in causing nervousness for the unit holders of ACMF and in fact caused redemption of units and the consequent fall in AUM
- 7.29 Admittedly, Shri Arora was managing the equity funds of ACMF. He claims to have had no role to play in the management of debt funds of ACMF. In such a scenario, the rationale for the unit holders of debt funds withdrawing their

investment, as stated by Shri Arora, can only be conjectures and surmises and do not merit any consideration.

- 7.30 It was a general perception that Alliance Mutual Fund and Shri Samir C Arora were almost synonymous. Hence, the un-denied rumors / reports of his impending exit from ACMF would have led to redemptions in the fund either from debt or from equity schemes. Further from the presentation made by Blackstone group to the bidders I find that the image of the Fund was dominated by the perception about fund management of Shri Samir C. Arora. Therefore, the contention of Shri Samir C. Arora that he was managing only the equity assets of ACMF and not the debt assets of ACMF and therefore any fall in debt assets cannot be attributed to him is not convincing.
- 7.31 I find no merit in the argument that there is no material correlation between the fall in the AUM of ACAML and fall in the NAV of the schemes of ACMF. It is a well known fact that when there is significant and unprecedented redemption pressure and consequent distress/ urgent sale of assets to meet the redemption pressure, the value realized from such sale of assets would be sub-optimal. It is common that sale of assets under distress condition fetches much lesser value than what it would have fetched if sold under normal circumstances/ at appropriate time.
- 7.32 Shri Arora has contented that all the equity schemes of ACMF (except Alliance Buy India Fund Scheme) have outperformed their relevant benchmark indices. A perusal of the performances of the benchmark indices, as furnished by Shri Arora, himself, reveals that each of the benchmark indices taken for comparison with the relevant equity schemes of ACMF have given negative returns during the relevant period (December 2, 2002 to January 31, 2003). It is also seen from reply of Shri Arora that all the equity schemes of ACMF (except Alliance Basic Industries Fund, Alliance Capital Tax Relief '96 and Alliance Front Line Equity Fund) have given negative returns to the unit holders during the relevant period. By arguing

- that the funds managed by him gave a lesser negative return to the unit holders when compared with their respective benchmark indices, Shri Arora is attempting to show that the unit holders of ACMF have not suffered losses. The paradox in such argument is obvious and does not deserve any further comment.
- 7.33 Shri Arora has chosen to compare the performance of certain schemes of ACMF with purportedly comparable schemes of certain other mutual funds. He has thereby attempted to show that the performance of the funds managed by him was superior to that of purportedly comparable schemes of such mutual funds. On the other hand, I find that similar comparisons with the schemes of certain other comparable mutual funds show an opposite picture.
- 7.34 During the period from December 02, 2002 to January 31, 2003, 4 equity schemes of ACMF viz. Alliance 95, Alliance Equity Fund, Alliance New Millennium Fund and Alliance Buy India Fund showed a decline in their respective NAVs. During the same period the equity fund scheme of HDFC Mutual Fund, one of the major Mutual Funds in India showed an increase of over 6.5% in the NAV. Similarly the NAV of K Balance Fund of Kotak Mahindra Mutual Fund showed an increase of over 4%.
- 7.35 In the light of the above, I do not find the contention of Shri Arora tenable that the performance of the funds managed by him was superior to that of other leading Mutual Funds during the referred period.
- 7.36 Shri Samir C Arora has argued that SEBI itself has envisaged a framework for exit by investors when there is a change in management. The regulation cited by him is meant to provide an exit option for the unit-holders in the event of any change in the controlling interest of the asset management company. To cite the said regulation in defence of his deliberate actions/inactions to cause redemption is at best sophistry.

7.37 The example of Zurich Mutual Fund cited is not comparable with the present case. The agreement for takeover of Zurich Mutual Fund by HDFC Mutual Fund was entered into on March 31, 2003 and the merger actually took place in the month of June 2003. The AUM of Zurich as on March 31, 2003 was Rs.2685.91 crores and the AUM on May 31, 2003 was Rs.3312.98 crores. In the case of Zurich, the merger actually happened and post decision of merger the AUM actually increased whereas in the case of ACMF the proposed stake sale did not take place and there was a fall of 35% in 2 months in the AUM to the tune of Rs.1332.32 crores during December 2, 2002 to January 31, 2003 i.e. when the bidding process was active.

7.38 The example of Sun F&C Mutual Fund is obviously not comparable with that of ACMF due to the much smaller AUM of Sun F&C Mutual Fund.

7.39 As discussed in the earlier paragraphs, the conduct of Shri Arora not only led to the decline in the AUM of ACMF but also resulted in steep decline in the NAVs of various schemes of ACMF thereby adversely affecting the interests of small investors. The argument that the fall in AUM would only affect the fee payable to Asset Management Company, which will benefit the small investors, whose interests SEBI is expected to protect, is fallacious. The following table indicates the sudden fall in AUM.

| <b>Dated</b> | <b>Equity (Rs.)</b> | <b>Debt (Rs.)</b>   | <b>Total (Rs.)</b>  |
|--------------|---------------------|---------------------|---------------------|
| 31-Jul-02    | 10,577,027,263.8600 | 23,838,599,623.7500 | 34,415,626,887.6100 |
| 30-Aug-02    | 11,213,525,445.9600 | 25,786,843,774.2662 | 37,000,369,220.2262 |
| 30-Sep-02    | 11,586,693,421.7000 | 23,958,443,114.4529 | 35,545,136,536.1529 |
| 31-Oct-02    | 10,959,015,017.5600 | 26,484,535,767.2171 | 37,443,550,784.7771 |
| 29-Nov-02    | 10,990,709,900.9900 | 26,070,199,919.0165 | 37,060,909,820.0065 |
| 31-Dec-02    | 10,685,481,962.0400 | 22,089,917,117.2886 | 32,775,399,079.3286 |
| 31-Jan-03    | 8,397,832,600.5300  | 15,689,938,057.5208 | 24,087,770,658.0508 |
| 28-Feb-03    | 8,330,578,941.3000  | 17,259,862,234.8864 | 25,590,441,176.1864 |
| 31-Mar-03    | 7,582,853,141.5200  | 14,430,757,923.8098 | 22,013,611,065.3298 |
| 30-Apr-03    | 7,790,875,139.8500  | 15,639,811,112.3890 | 23,430,686,252.2390 |
| 30-May-03    | 8,281,246,494.2000  | 16,001,214,811.1705 | 24,282,461,305.3705 |

**Note:** The above AUM does not include the corpus of Term Plans which is launched by ACMF every week on Wednesday.

- 7.40 As per the computation of SEBI the unit holders of Alliance New Millennium Fund suffered a loss of about Rs.12 crores and those of Alliance Buy India Fund suffered a loss of Rs.3.36 crores during the period from December 2, 2002 to January 31, 2003. Shri Arora in his reply has merely quibbled over the methodology of computation adopted by SEBI. He has neither indicated alternative methodology of computation nor indicated a figure different from that given by SEBI. For argument's sake, even if an alternative methodology is applied yielding a lower / higher figure for the losses suffered by the unit-holders, the liability of Shri Arora for having caused such loss still remains. Hence the reply of Shri Arora lacks any merit.
- 7.41 As discussed in the earlier paragraphs Shri Arora indeed is found to be responsible for the redemption pressure and the fall in NAV and the consequent loss suffered by investors. A mere denial of liability of Shri Arora will not suffice. The chain of events relating to the stake sale proposal of Alliance Capital has been set out in the SCN in a chronological manner and not in any special manner as insinuated in the reply of Shri Arora.
- 7.42 The role played by Shri Arora in 'thwarting' the plan of Alliance Capital to sell ACAML has been discussed elaborately in earlier paragraphs and do not require repetition. The 'selfish motive' of Shri Arora has been brought out clearly in the form of personal gain (in terms of crores of rupees) he stood to make if his bid along with Henderson was successful. These charges are not vague and incoherent as alleged in the reply of Shri Arora.
- 7.43 Shri Arora did play a role in causing uncertainty and confusion in the minds of investors relating to his continuance. Such uncertainty and confusion resulted in unprecedented and large scale redemptions by the unit-holders which in turn resulted in loss in NAV and consequent losses to the unit-holders. I find the

allegations of SEBI logical and supported by adequate evidence. From the aforesaid discussion, I do not concur with the contention that Shri Arora had no role to play in the events relating to the proposal of stake sale by Alliance Capital.

7.44 I find that there is an inherent flaw in the denial by Shri Samir C Arora of conflict of interest on the ground that his bidding was done transparently and after informing the management of Alliance Capital. As a Fund Manager, it was paramount responsibility of Shri Samir C. Arora, to enhance the AUM of the mutual fund for the benefit of the Unit holders. However, in contrast, in his role as a bidder, his interest would have been to acquire the fund at the cheapest possible price. From the subsequent events it is observed that by his actions/inactions, Shri Samir C Arora has let the AUM fall, knowing that the valuation of the AMC depend on AUM, so as to achieve his selfish objective of acquiring the fund along with Henderson at a lesser price and in the process he has compromised his position of fiduciary responsibility with unitholders and the sponsor. Therefore, there can be no doubt that the acts of Shri Samir C. Arora were directly in conflict with his interest as a Fund Manager. In consonance with the well recognized ethical principles, Shri Samir C Arora should have resigned as Fund Manager of ACMF before proceeding to bid for buying the stake in ACAML to avoid any conflict of interest. ACAML, too, should have sought his resignation before submission of his bid along with Henderson.

7.45 Having bid for the stake of Alliance Capital in ACAML, it is strange on the part of Shri Arora to claim that he was never a part of the sale process. He did tie up with Henderson and bid for ACAML. He did inform the management of Alliance Capital about his bid. Apparently, the other bidders were also kept informed about the fact that Shri Arora has made a bid for ACAML along with Henderson. Whether he had any direct or personal interactions with the persons (whether belonging to Blackstone group who were the merchant bankers or the management of Alliance Capital or with other bidders) involved in the sale process does not have any bearing on the charges leveled against Shri Arora.

- 7.46 The parallel sought to be drawn between Shri Arora's bid (along with Herderson) for acquiring ACAML and "Employees' Stock Option"/ 'Management Buy Out' smacks of perversity, designed to distract. While the Employees Stock Option is an option granted to employees of a company to buy its shares as a part of incentive scheme to align the interest of employees with those of the shareholders, 'Management Buy Outs', which began in the USA during 1960s and gained currency elsewhere refers to a corporate finance activity whereby the existing 'management' with outside financial backing/ leveraging buy the business, in certain circumstances like impending bankruptcy of the company or its parent; death of the current owner (promoter), privatization, etc. Viewed in the light of the facts of the instant case, Shri Arora's bid to buy ACMF, in terms of motive and intent, is, in my view, incomparable either to the exercise of Employees' Stock Option or to management buy out plan. In any case, I find that Shri Arora's bid for acquiring ACAML is itself not being questioned and what is called into question is the conduct of Shri Arora, as a professional fund manager, in the matter of the said bidding.
- 7.47 I find that During December 2002 – January 2003 when the bidding process for ACAML was in progress no clarification of any sort regarding the position of Shri Arora and his role in the stake sale process was given to the unit-holders. There were media rumours and speculations resulting in uncertainty. I find that if the position of Shri Arora in the context of stake sale proposal was clarified, there should not have been any confusion in the minds of unit-holders of ACMF.
- 7.48 As contended by Shri Samir C Arora, I do not find anything in the SCN to indicate that the interim actions against Shri Arora were taken based on press and media reports rather than on specific facts ascertained pursuant to detailed investigations. The first para of SEBI's SCN dated Feb. 20, 2004, merely states the background in which the investigations were initiated. When the investigations were in progress it became apparent to SEBI that Shri Arora had,

prima-facie, violated the provisions of SEBI Act, Rules and Regulations made there-under. Considering the gravity of the violations committed by Shri Arora and the emergent need to protect the interest of investors from further harm, likely to be caused by continued dealings of Shri Arora, interim directions as deemed appropriate at that time were passed by me, pending further investigations.

- 7.49 Shri Arora is now attempting to belittle his role in ACMF by claiming that he was managing over USD 1 billion in equity assets of nine Asian countries and the assets of ACMF were only about USD 250 mn thereby insinuating that the Indian portfolio was only a small portion of the total funds under his management. However, the fact that Shri Arora had bid for the stake of ACAML and was willing to re-locate to India to manage the funds of ACMF, if his bid along with Henderson was successful, shows that the Indian portfolio and ACMF formed a significant part in the scheme of things of Shri Arora.
- 7.50 While Shri Arora has made a mountain out of a mole hill regarding the manner in which an isolated statement of his is found to have been recorded, he has not denied the veracity thereof. In any case, I do not find any need to rely upon it. There are enough evidence otherwise to show that he stood to gain substantially from his joint bid along with Henderson.
- 7.51 I find that in terms of regulations 2(1) (e) of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 ACMF and ACM are persons acting in concert. Further, I also find that Shri Arora manages the funds belonging to the ACMF and ACM. Therefore, their shareholding in various companies are to be aggregated inter alia for the purposes of disclosure requirements under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 and SEBI (Prohibition of Insider Trading) Regulations, 1992. Hence, the contention of Shri Arora that ACMF, Alliance Capital and its FIIs and sub-accounts are not persons acting in concert is not tenable.

- 7.52 The submissions referred to by Shri Arora in his reply probably refer to his submissions dated Aug. 27, 2003 to SEBI. The referred submissions of Shri Arora were made in response to an earlier proceedings and not with reference to the present SCN of SEBI. In any case, I do not find any merit in the arguments contained in the said submissions with regard to the instant charge. The charge relates to the role of Shri Arora in the non-disclosures / wrongul disclosures made by ACMF under the Takeover Regulations and Insider Trading Regulations and does not deal with the reporting relationship of the compliance officer with the fund manager.
- 7.53 I find that Shri Samir C Arora was the only person who was aware about the combined share-holding of ACMF and ACM in various companies. Further, it is also observed that Shri Samir C Arora has failed to disclose the combined share-holding of ACMF and funds belonging to ACAML. The aforesaid failure on the part of Shri Samir C Arora has resulted in inadequate disclosures by the ACAML in terms of SEBI (Substantial Acquisition of shares and Takeovers) Regulations, 1997 and SEBI (Prohibition of Insider Trading) Regulations, 1992.
- 7.54 I agree that under any provisions of securities law, compliance requirements was not the fund manager's responsibility. However, I note that Shri Samir C. Arora being key personnel of a mutual fund should have conducted himself professionally and ensure compliance with the Mutual Fund Regulations in letter and spirit. Hence, the contention of Shri Arora that there is no basis for levying such a charge against him is not tenable.
- 7.55 In the above reply, Shri Arora himself has stated, rightly so, that the presumption of persons deemed to be acting in concert is rebuttable. In the absence of rebuttal, SEBI is entitled to presume that the said entities are acting in concert. Shri Arora's attempt to cast the obligation on SEBI to positively show that the said entities were persons deemed to be acting in concert does not stand scrutiny.

In any case, as seen from the succeeding paragraphs, SEBI indeed has shown the said entities as persons acting in concert.

- 7.56 I note that Shri Arora was taking investment decisions on behalf of ACMF and various FIIs/sub-accounts belonging to ACM. Thus, it goes without saying that Shri Arora was aware of the holdings in various scrips of ACMF and the FII/sub-accounts on whose behalf he was making investment decisions. Being aware of the holdings in various scrips by the individual holdings, calculation of combined holdings requires simple addition, which, I presume, is not beyond Shri Arora's capacity.
- 7.57 I note that while quoting the SEBI's letter dated 30.5.2001 to ACAML, Shri Arora has conveniently ignored the last sentence of the said communication, which reads 'However, please note that the Takeover Regulations should be complied with in letter and spirit.' I note that the clarification of SEBI would not hold good if the conditions subject to which such clarification was given is not adhered to. It is a fact that Shri Arora was managing the investment management functions of both ACMF and the FII/sub-accounts belonging to the associate of sponsor.
- 7.58 Shri Arora has claimed that there was indeed a Chinese wall between the compliance function and Shri Arora's fund management operations. I find that this contention of Shri Arora is only an attempt to divert attention from the charge of SEBI that there was no Chinese wall between the fund management operations of ACMF and the affiliates of the sponsor of ACMF.
- 7.59 While it is true that primarily it is the responsibility of ACAML and ACM to comply with the disclosure requirement in terms of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations and SEBI (Prohibition of Insider Trading) Regulations, Shri Samir C. Arora cannot be totally absolved of his responsibility as a professional and a key functionary to advise the ACAML and ACM to

comply with the regulatory requirements. I have noted that adjudication proceedings have already been initiated against ACM and ACAML for the said violations. In view of this I do not consider it necessary to give conclusive finding in these proceedings on violation of the provisions of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations but hold Shri Samir C. Arora guilty of professional misconduct for the reasons stated above.

7.60 It is true that the code of conduct as specified in the MF regulations is applicable to the mutual funds, the AMC and the Trustees. However, the various acts of omission and commission by Shri Arora resulted in the violation of code of conduct by the said entities. Hence Shri Arora cannot escape responsibility stating that the code of conduct is not applicable to him. The compliance of the Regulations by the Mutual Fund inter alia depends on the honest discharge of duties by the persons in key positions in the Fund. Shri Samir C Arora, being in the key position as a fund manager is guilty of professional misconduct.

7.61 Clause 1 of Code of Conduct in terms of Fifth Schedule to the SEBI (Mutual Funds) Regulations 1996 mandates that Mutual fund schemes should not be organized, operated, managed or the portfolio of securities selected, in the interest of sponsors, directors of asset management companies, members of Board of trustees or directors of trustee company, associated persons as in the interest of special class of unit-holders rather than in the interest of all classes of unit-holders of the scheme. Shri Samir C Arora was managing the equity portfolio of ACMF and at the same time he was also managing the Indian allocation of FII/sub-accounts belonging to ACM. While doing so, he managed the portfolio of securities in the interest of sponsors and to the detriment of the unit-holders of ACMF, thereby he aided and abetted the violation of the above clause by the trustees and Asset Management Company of ACMF.

7.62 Clause 4 of Fifth Schedule of Code of Conduct states that Trustees and asset management companies must avoid conflicts of interest in managing the affairs of

the schemes and keep the interest of all unit-holders paramount in all matters. In bidding for the stake of ACAML in collaboration with Henderson, Shri Samir C Arora placed himself in a position of conflict of interest and thereby, he aided and abetted the violation of Clause 4 by ACAML and ACAM Trust Co Ltd.

- 7.63 Shri Samir C Arora's aforesaid conduct in aiding and abetting the Trustees and AMC of ACMF in violating the various provisions of SEBI (Mutual Funds) Regulations 1996, cited above is detrimental to the interest of investors and the orderly development of the Securities Market.
- 7.64 SEBI has already initiated Enquiry proceedings against Alliance Capital . Hence I do not find any merit in the contention of Shri Arora that SEBI has entirely blamed only Shri Arora. Alliance Capital, if found guilty of violating Mutual Fund Regulations shall be penalized in accordance with the law.
- 7.65 From the aforesaid discussions and several instances of actions or inactions on the part of Shri Samir C. Arora (as narrated above) it becomes abundantly clear that Shri Arora is guilty of grave professional misconduct which calls for prompt remedial action from SEBI under Sections 11(4) and 11B of the SEBI Act to protect the interests of investors and integrity of the Indian securities market. SEBI shall be failing in its bounden duty if it does not take note of such professional misconduct and take appropriate action.

**Second issue:**

- 8.1 Whether Shri Samir C Arora is guilty of violating the provisions of Regulation 4(a), 4(b), 4(c), 4(d) and 5 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995 ?
- 8.2 Shri Samir C Arora contended that the terms 'significant holding' and 'low floating stock' are vague and subjective terms. In my considered view the term 'significant holding' needs to be seen in relevant context. For instance SEBI

(Prohibition of Insider Trading) Regulations 1992 considers 5% share-holding as significant share-holding and a 2% variation as significant variation in holding. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations 1997 considers various shareholdings such as 5%, 10%, 15% etc. as significant. Similarly 'low floating stock' also requires contextual interpretation. In the context of the charges against Shri Arora, the terms 'significant holding' and 'low floating stock' have been used to show that the fund managed by Shri Arora had a substantial percentage of the floating stock of the said companies and was in a position to influence the market trading (both prices and traded volumes) of the respective scrips.

- 8.3 Shri Arora has contended that all the charges in relation to these stocks relating to the purported benefits being conferred on the offshore funds to the detriment of the domestic mutual fund, are levelled in hindsight. However I find that the said charge has been made upon analysis of trading pattern, which reveals such a bias. Hence, there is no merit in the contention of Shri Arora that the charges have been levelled in hindsight. Whether Shri Arora had such thought processes (of benefiting the investors of sponsor funds to the detriment of unitholders of ACMF) while making the investments on behalf of off-shore funds and ACMF can only be determined from the analysis of his trading pattern. Such an analysis by SEBI does reveal numerous instances wherein Shri Arora had dealt in various scrips in a manner that favoured the investors of off-shore funds (associates of sponsor of ACMF) to the detriment of the unit-holders of ACMF.
- 8.4 Whether Shri Arora was offered differential compensation aimed at selectively helping the performance of the so-called sponsor/FII funds or whether he was compensated in any other manner does not seem to be relevant. Whereas the trading done by Shri Arora in various scrips on behalf of off-shore funds and ACMF is a bare fact and the actual figures relating to such trading incontrovertibly show that the trading pattern of Shri Arora did benefit the

investors of FII/sub-accounts who were the associates of sponsor to the detriment of the unit-holders of ACMF.

- 8.5 With regard to the contentions of Shri Samir C Arora regarding market impact of transactions done by him, it must be clarified that the correct comparison would be between the opening price on Sep. 6, 2001 (i.e. the date of commencement of sale of BTL shares by funds managed by Shri Arora) and the closing price on Sep. 11, 2001 (i.e. the date of completion of sale by Shri Arora). Since, in the normal course, there is negligible difference in prices between NSE and BSE, with a view to avoid citing too many numbers and thus maintain clarity in the discussions, the prices on NSE alone have been reckoned to examine the impact of above trades.
- 8.6 On Sep. 6, 2001, ACMF and ILF had together sold 4,15,600 shares of BTL. The price of the scrip of BTL which opened at Rs.223/- and touched a high of Rs.229/- at NSE on Sep. 6, 2001, closed at a much lower Rs.216.75. Thus, it is incorrect to say that the selling by Alliance Capital did not depress the price of the scrip.
- 8.7 On September 11, 2001, ACMF and ILF together sold 2,19,700 shares of BTL. The price of the scrip on NSE on Sep. 11, 2001 opened at Rs.220.10, touched a high of Rs.229.40; but closed lower at Rs.226.55. Thus, the sale by ACMF and ILF did depress the price of the scrip.
- 8.8 Delivery based transactions impact the price of a scrip in a significant manner as compared to square off transactions. Hence, it is pertinent to compare the trades by Shri Arora with the delivered quantities on the exchanges on the respective dates. Only a small portion of shares traded in the market get delivered. Hence it is clear that the sales by ACMF and FII sub-accounts of Alliance Capital constituted a significant portion of the market delivered quantities on Sep. 6, 2001 and Sep. 11, 2001.

- 8.9 It is clear that the sales by funds managed by Shri Arora did form a significant portion of the market delivered quantity and these sales cannot be ignored as being insignificant. Shri Arora himself has in his submissions (page 30 – table containing summary of factual allegations) admitted that SEBI has not mentioned the name of the seller on Sep. 19, 2001. He himself has wrongly inferred that SEBI has meant that NTC or any FII/sub-account has made the sale on Sep. 19, 2001 and has taken pains to deny the same. SEBI is aware that the seller on Sep. 19, 2001 was indeed ACMF.
- 8.10 While Shri Arora has taken pains to point out that the purchase on Sep. 19, 2001 was on behalf of ACMF and the sponsor funds (i.e NTC) purchased later (i.e. on Sep. 26 & 27, 2001), he has conveniently failed to mention that while the purchase on behalf of ACMF was done by him at Rs. 186.42, the purchase on behalf of NTC on Sep. 26 & 27, 2001, have been done at Rs.174.50 and Rs.174.68 respectively. Thus the purchase on behalf of the sponsor fund has been done by Shri Arora at a substantially lower price (the price differential works out to about Rs.12/- per share). This must be looked at in the context of a total 5,71,778 shares of BTL were purchased by ACMF and the FII taken together during Sep. 19, 26 & 27, 2001. Elementary mathematical calculation shows that the acquisition cost of BTL shares for FII / sub-accounts is lower by a few lakhs rupees when compared to the acquisition cost of ACMF.
- 8.11 Further, it is essential to examine the trading pattern over the entire period cited by SEBI ie. From Sep. 6, 2001 to Oct. 10, 2001 in totality, to arrive at a conclusion regarding any bias in favour of FII/sub-accounts to the detriment of ACMF. In this context I note that on Sep. 6 and 11, 2001, ACMF and FII sub-accounts have together sold 6.35 lakhs shares of BTL at prices ranging from Rs.220.53 to Rs.227/-. The price of the scrip fell. Thereafter, while ACMF purchased 3.92 lakhs shares of BTL at Rs.186.42 on Sep. 19, 2001 and NTC purchased 1.80 lakhs shares of BTL at about Rs.174.60 on Sep. 26 and 27, 2001. Thereafter on Oct. 8 and 10, 2001, Shri Arora purchased 40,000 shares and

1,50,000 shares at Rs.181.80 and Rs.212.40, on behalf of ACMF. Thus, it is seen that the purchases on Sep. 19, 2001, Oct. 8 and 10, 2001 on behalf of ACMF have been at significantly higher prices than those on behalf of NTC on Sep. 26 and 27, 2001.

8.12 The above trading pattern shows that ACMF and sponsor FII/sub-accounts initially sold the shares of BTL. Such sale did depress the price of scrip. Thereafter the sponsor FII/sub-account have purchased back the shares at a price much lower when compared to that at which ACMF bought back the shares. Therefore, I do not find any merit in the denial of Shri Arora.

8.13 The impact of sale or purchase on any day ought to be examined by comparing the opening, high, low and closing price on the exchange (say, NSE) on the same day (of course with due regards to the percentage of concentration of such purchase or sale compared to the market quantities). I find that the scrip of BTL on Sep. 19, 2001 opened at Rs. 179, reached a low of Rs.163/-, touched a high of Rs.190.30 and closed at Rs.187.05. Thus, the price of the scrip did close higher on Sep. 19, 2001 when compared to the opening price on the day. Even if Shri Arora's inappropriate technique of comparing with the previous day's closing price is reckoned for analysis, I note that the scrip closed at Rs.176.20 on Sep. 18, 2001; thus, the closing price on Sep. 19, 2001 was any way higher than the opening price on that day (or the closing price on the previous day). This shows that the above contention of Shri Arora that the price continued to fall despite his purchase is not correct and misleading.

8.14 The assets under management under the equity schemes of ACMF on January 15, 2003 and January 31, 2003 (which was a Friday) were Rs.1002.13 crores and Rs.839.78 crores. During this period i.e. from Jan 15, 2003 to Jan 31, 2003 there was a steady decline in the AUM of equity schemes of ACMF. Assuming, for the sake of argument, that the sales of HTMT shares during Jan. 16 to 29, 2003 were done indeed to meet the redemption pressure, as contended by Shri Arora, I note

that the funds available to Shri Arora for investment on behalf of ACMF on Feb. 3, 2003 (which was a Monday) were lower than that on Jan. 16, 2003 when he sold the shares of HTMT purportedly to meet the redemption pressure. Hence, the reason proffered by him for the reversal of his earlier decision and the purchase on Feb. 3, 2003 does not appear to be credible.

8.15 Delivery based transactions impact the price of a scrip in a significant manner as compared to square off transactions. Hence, it is pertinent to compare the trades by Shri Arora with the total delivery on the exchanges on the respective dates. Accordingly, a comparison of the trades by Shri Arora with the delivered quantity on NSE reveals the following: On Jan. 24, 2003, ACMF sold 24, 000 shares of HTMT constituting 6% of the market delivered quantity. On Jan 27, 2003, ACMF sold 20,000 shares of HTMT constituting about 5% of the market delivered quantity. On Feb. 3, 2003, the purchases by the funds managed by Shri Arora, totaling 3,28,000 shares, constituted as much as 45% of the market (BSE+NSE) delivered quantity of 7,30,125 shares. Thus, the trades by the funds managed by Shri Arora in the scrip of HTMT, on the above dates, is not insignificant as contended by Shri Arora.

8.16 On certain of the above dates, the sale by Shri Arora as a percentage of the market delivered quantities were indeed small. In this context, I note that the media routinely publicize information regarding institutional purchases and sales in various scrips. The continuous sale by Shri Arora during the period from Jan. 16 to 29, 2003 (in significant quantities on certain dates) would also get reported as sales by Mutual Fund thereby resulting in a negative influence on the price of the scrip. Hence, the contention of Shri Arora that his above sales were not significant enough to send a negative price signal does not have any merit.

8.17 I find it is pertinent to compare the trades by Shri Arora with the total delivery on the exchanges on the respective dates. Compared to the delivered quantities on NSE and BSE, the sale of 1,75,000 shares of Mastek by ACMF on Jul. 25, 2002

constitutes 39.14% of the market delivered quantity of 4,47,135 shares, which is definitely not miniscule as contended by Shri Arora.

- 8.18 The market (BSE+NSE) delivered quantities in the scrip of Mastek on Jul. 29, 30 & 31, 2002 were 2,94,219 shares, 3,88,162 shares and 4,15,245 shares respectively. The purchase of 1,00,000 shares, 2,00,000 shares and 2,20,000 shares by ACMF and FII sub-accounts on Jul. 29, 30 & 31, 2002 respectively constitutes 34%, 52% and 53% of the said delivered quantities on the market. The above purchases by funds managed by Shri Arora is not miniscule as contended by Shri Arora.
- 8.19 As regards the actual impact on price Shri Arora has cleverly compared the closing price on Jul. 25, 2002 with the closing price on previous day; while the correct comparison would be between the opening and closing prices on Jul. 25, 2002. It is seen that the scrip opened at Rs.368.95 on Jul. 25, 2002 and touched a high of Rs.384.75 before closing at a much lower price of Rs.373.60. I do note that the closing price on Jul. 25, 2002, was slightly higher compared to the opening price albeit by a marginal 1.2%; but it cannot be ignored that the scrip of Mastek had risen significantly (by about 4.3%) during the intra day trade on Jul. 25, 2002 and the closing price was depressed by the huge quantities sold (constituting about 40% of the market delivery) by Shri Arora on behalf of ACMF.
- 8.20 Whether the sale on Jul. 25, 2002 was done with a view to hide the intention to acquire these shares at a subsequent date, at a lower price, can only be determined by examining Shri Arora's subsequent behaviour i.e. whether indeed he purchased back the shares at a proximate date. I find that this was indeed the case. Shri Arora did buy back the shares of Mastek on dates proximate to Jul. 25, 2002. Shri Arora has bought back the shares on Jul. 29, 30 & 31, 2002. Significantly these shares were indeed bought back (on behalf of both ACMF and off-shore

funds) at lower price (Rs.323 to Rs.358/-) when compared to the price at which ACMF had sold these shares earlier (at Rs. 372.32 on Jul. 25, 2002).

- 8.21 I note that between Jul. 25, 2002 when Shri Arora had sold the shares of Mastek (on behalf of ACMF) and Jul. 31, 2002 when he had subsequently bought back the shares, the price of the scrip had fallen from Rs.368.95 to Rs.349.85. Hence I find the claim of Shri Arora that the price in fact moved up and profits were made is false and baseless. In this scenario, whether he did diligently discharge the mandate and duty of a fund manager to ensure the best interests of the unit-holders is a moot point.
- 8.22 Shri Arora has claimed that the price does not react to the purchases made by him since despite purchases between Jul. 29 and 30, 2002, the price continued to fall. Hence, he claims, that the sales or purchases effected by him did not have a corresponding impact on the price. I find that on NSE the scrip of Mastek opened at Rs.355.30 on Jul. 29, 2002 and closed at Rs.362.95 (High and low prices were Rs.366.95 and Rs.351.25). Thus, on Jul. 29, 2002, the price indeed went up by 2.15%. On Jul. 30, 2002 the scrip opened at Rs.371/- and closed at Rs.352.35 (High and low prices were Rs.376/- and Rs.346.70). I note that there was significant selling pressure in the scrip of Mastek on Jul 30,2002 as evidenced from the fact that the scrip which had opened at Rs.371/- had touched a low of Rs.346.70 ( a fall of 6.5%). However, the scrip recovered from the above low price and closed higher at Rs.352.35. It is clear that the scrip has moved down when Shri Arora has sold on Jul. 25, 2002 and moved up when he purchased on Jul. 29 and 30, 2002. Hence I do not find any merit in the contention of Shri Arora that the sales or purchases effected by him did not have a corresponding impact on the price. Consequently, the charge of moving the price upwards or downwards cannot be said to be baseless.
- 8.23 It is stated that SEBI regulations do not prohibit, selling in a day when purchase is made earlier in the day. This again is a devious argument. While intra-day

- delivery based buying and selling of a scrip by a Mutual Fund is unobjectionable, what is queer to note is that Shri Arora has sold 50,000 shares of Mastek on net basis on behalf of ACMF while he has purchased 2.50 lakhs shares on behalf of off-shore funds on the same day. Thus there was obvious contradiction of view taken by him while making trading decisions on behalf of ACMF and the off-shore funds.
- 8.24 While ACMF purchased 1.50 lakhs shares and sold 2.0 lakhs shares of Mastek on Aug. 23, 2002, the off-shore funds bought 3 lakhs shares and sold 50,000 shares on the same day. In view of the fact that ACMF has sold much larger quantities (4 times that of off-shore funds), it is misleading to compare the absolute profits earned by ACMF with that of off-shore funds and reach a conclusion that ACMF benefited more than the off-shore funds.
- 8.25 The funds managed by Shri Arora (i.e. ACMF and the off-shore funds) had bought and sold huge quantities of the shares of Mastek on the same date i.e. Aug. 23, 2002. On gross basis, the above trades of the entities managed by Shri Arora constituted as much as 97% of the delivered quantities on the market. In other words, if these trades on excluded the deliverable quantity in the market is negligible. On a net basis, one entity (ACMF) had a sale position while other entities (off-shore funds managed by Shri Arora) had a purchase position. At least a portion of the deliveries received by the off-shore funds had to be from the deliveries given by ACMF (albeit through the exchange settlement mechanism). Thus, there was indeed creation of artificial trading volumes caused by the trades of Shri Arora on behalf of various entities managed by him.
- 8.26 I agree that both mutual funds and FIIs can trade only on a delivery basis and have to deliver or take delivery of every single sale and purchase made by them. However, this would not be a constraint for Shri Arora as ACMF and off-shore funds had the necessary shares (as Aug. 22, 2002, ACMF and the off-shore funds together held 9.57 lakhs shares of Mastek representing about 7% of the equity

- capital of Mastek) and funds for delivery. The above has been cited as an example to show that the requirement of giving and taking delivery for every single purchase and sale could have been a constraint for Shri Arora since the entities managed by him had the requisite shares as well as funds.
- 8.27 Sale by a fund manager with a view to book profits when price of a scrip has increased is understandable. It is surprising that on Oct. 1, 2002 and Oct. 3, 2002, Shri Arora sold 4.60 lakhs shares and 1.85 lakhs shares respectively of Mastek on behalf of ACMF and FII/ sub-accounts citing the reason that price had fallen. Even if it is presumed that such sale made on October 3, 2001 at about Rs.381/- as a stop loss measure, then the subsequent purchase of the same shares the very next day i.e. October 4, 2002 at an even higher price of Rs.388-389/- does not stand to reason, notwithstanding the research report by an analyst who was a member of the team led by him.
- 8.28 Further, while the sale on Oct. 3, 2002 was made only by ACMF, the shares were bought on Oct. 4, 2002 by both ACMF and PACs. While the sale on Oct. 1, 2002 and Oct. 3, 2002 constituted 74% and 42% respectively of the market delivered quantities of 6,20,087 shares and 4,37,956 shares, the purchases on Oct. 4, 2002 by ACMF and the off-shore funds managed by Shri Arora constituted about 76% of the market delivered quantity of 8,76,714 shares. Hence, the argument that his trades were miniscule and there was no creation of artificial volume is not acceptable.
- 8.29 It is pertinent to compare the trades by Shri Arora with the total delivery on the exchanges on the respective dates. In this context, I also note the earlier contention of Shri Arora that the entities managed by him (i.e. Mutual Fund and FII/ sub-accounts) had to necessarily give and take delivery of every single purchase and sale made by them.

- 8.30 The total delivered quantities on the market (BSE and NSE taken together) in the scrip of Mastek on Aug. 23, 2002 were 7.22 lakhs shares. I observe that the entities managed by Shri Arora on Aug. 23, 2002 together bought and sold 6.50 lakhs which constituted as much as 97% of the delivered quantities on the market. While the sale on Oct. 1, 2002 and Oct. 3, 2002 constituted 74% and 42% respectively of the market delivered quantities of 6,20,087 shares and 4,37,956 shares, the purchases on Oct. 4, 2002 by ACMF and the off-shore funds managed by Shri Arora constituted about 76% of the market delivered quantity of 8,76,714 shares. Hence the contention of Shri Arora that the contribution to the volumes by the impugned transactions (i.e. on Jul. 25, 29, 30 and 31, 2002, August 20, 22 & 23, 2002, Oct. 1, 3 & 4, 2002) is far too minor and therefore, the allegation relating to purported creation of artificial volumes simply cannot be levelled, is not tenable.
- 8.31 The contention of Shri Arora that the price of the scrip of UPL steadily moved up during the period from Oct. 1, 2002 to Oct. 18, 2002 is factually wrong. On October 1, 2002, the price of UPL on NSE opened at Rs. 154.60 and closed at Rs.153.25. On October 18, 2002, the scrip opened at Rs.172.55 and closed at Rs.168.75. In fact during the period Oct. 1 to 18, 2002, only on three trading days (Oct. 7, 8 & 10, 2002), the price of the scrip closed higher than its opening price on the respective days. The factual mistake of the contention of Shri Arora apart, the relevant portion of the SCN points to the apparently contradictory investment stance taken by Shri Arora when, on Oct. 10, 2002 he sold 2.84 lakhs shares at Rs.174/- held by ACMF while he simultaneously bought 1.00 lakhs at Rs.162.22 on behalf of ILF. Pointing to the price trend (that too incorrectly) over a period of 18 days (9 days before and 8 days after) does not negate the apparent contradiction cited above.
- 8.32 With regard to the dealings by funds managed by Shri Arora on Oct. 10, 2002, I note that the sale of 2.84 lakhs shares by ACMF constituted as much as 28% of

the market delivered quantity of 10,29,331 shares. When considered along with the purchase of 1.00 lakhs shares by ILF, the trades by the entities managed by Shri Arora (ACMF and ILF) together constituted as much as 37% of the market delivered quantity. The actual price movement on NSE on Oct. 10, 2002 also bears testimony to the impact of such a large sale and purchase by ACMF and ILF respectively. On Oct. 10, 2002 while the scrip opened at Rs. 154.85 on NSE, touched a high of Rs. 179.95; the price fell to Rs. 153/- before recovering to close at Rs.175.40.

8.33 I also note that Shri Arora in his reply has cleverly dealt with the price impact of the net sale position of ACMF and the off-shore fund taken together (by netting off the purchase and sale position) in stead of reckoning the gross trades which would have truly revealed how significant (as shown in the earlier paragraph) the quantities bought and sold by ACMF and ILF were compared to the market quantities.

8.34 Shri Arora has claimed that the sale of UPL shares on various dates during December 2002 to January 2003 were aimed at meeting the redemption pressure and was part of the orderly liquidation of assets in schemes where there were redemption requests. I note that these UPL shares have been sold from the portfolio of Alliance Equity Fund, Alliance Frontline Equity Fund and Alliance 95 schemes. However, the above-mentioned three schemes of ACMF have during the same period (i.e. December 2002 to January 2003) purchased 1.64 lakhs shares of Mastek. Thus, the contention that the sale of UPL shares were aimed at meeting redemption pressure is not tenable.

8.35 I note that, during December 2002 to January 2003, over a period of 14 trading days, ACMF sold about 2.72 lakhs shares of UPL at prices ranging from Rs.173.75 to Rs. 137.23. Compared to the market delivered quantities, the sale by ACMF constituted 1.09% to 62.95% on various dates. In 10 out of the said 14 trading days, the sale by ACMF constituted over 10% of the market delivered

quantity. Hence, I do not find the contention of Shri Arora that compared to the market quantities the sale by ACMF was negligible, tenable.

8.36 As regards price impact of such sales by ACMF, I note that during December 2002 to Jan. 2003, the price of the scrip of UPL on NSE declined from Rs.187.10 to Rs.134.65 i.e. a decline of about 28% in 2 months. On December 1, 2002, ACMF and ILF together held 19.80 lakhs shares of UPL constituting 7.77% of the capital of UPL. It is apparent that sale of large quantities of shares of UPL (as demonstrated earlier) by a significant share-holder viz. Alliance Capital, contributed to the fall in the price of the scrip. Hence the contention of Shri Arora that there was indeed no impact on the price owing to these sales is not tenable.

8.37 From the above trading pattern in the said five scrips it is seen that Shri Samir C Arora has indulged in manipulative transactions, inter alia, with the intent to artificially inflate/depress the prices of the scrip, to create false / misleading appearance of trading in the scrips in various scrips over a period of time and thus violated Regulation 4(a), 4 (b), 4 (c) &4 (d) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995, which read as follows:

“No person shall -

(a) effect, take part in or enter into, either directly or indirectly, transactions in securities, with the intention of artificially raising or depressing the prices of securities and thereby inducing the sale or purchase of securities by any person ;

(b) indulge in any act, which is calculated to create a false or misleading appearance of trading in the securities market;

(c) indulge in any act which results in reflection of prices of securities based on transactions that are not genuine trade transactions;

(d) enter into a purchase or sale of any securities, not intended to effect transfer of beneficial ownership but intended to operate only as a device to inflate, depress or cause fluctuations in the market price of securities.”

8.38 Further it is to be examined whether the statement of Shri Arora in an interview to Business Standard dated May 5, 2003 was misleading or not. I note that in the said interview with Business Standard, in response to a query, “What is your allocation to tech stock and how do you find the valuations?”, he inter alia replied “Digital Globalsoft – as per market rumours – may merge with HPISO in India, which will make it the sole subsidiary of a USD 70 billion plus IT company and therefore, be the obvious beneficiary of all the business that the parent can send to India, plus its normal business”. I find that his statement does not merely point out that a merger of DGL with HPISO was likely but also conveys a favourable view about the prospects of DGL post-merger.

8.39 Presuming for a moment that he did make the above statement in good faith, the issue of what prompted him to change his opinion 3 days later (as evidenced by his sale commencing May 8, 2003) needs to be addressed. The market definitely did not come to know of any adverse development relating to DGL during the period May 5, 2003 to May 7, 2003 as evidenced from the fact that the price of scrip (NSE) opened at Rs. 531.35 on May 5, 2003 and closed at Rs.597.25 on May 7, 2003. (I note that Shri Arora has in a later part contended that the interview was actually given on April 30, 2003 though it was published on May 5, 2003. Even if the prices on April 30, 2003 is reckoned, I note that the price of DGL has increased from Rs.531.35 on April 30, 2003 to Rs.597.25 on May 7, 2003 and thus the position does not change).

8.40 I find that when a journalist posed a general query to Shri Arora on his allocation to Tech stock and how he finds the valuations, he stepped out of context and brought the demerger issue of DGL. He went on to narrate the merits of the demerger with a motive of profit as he had a significant holding of DGL in the

portfolio managed by him. Admittedly he was selling the shares of DGL for the past several months and continued to do so subsequent to the said interview.

8.41 I find that Shri Arora himself has not denied that such a statement will induce transaction in securities. In any case, such a statement by a fund manager who, admittedly (in his submissions dated Aug. 27, 2003 to SEBI – Page 3 para 6(a)) is a reputed and successful fund manager and was internationally acclaimed, would indeed induce common investors to invest in the scrip. This clearly demonstrates that he misled the investors and induced them to buy the shares of DGL while he was disposing the same.

8.42 Considering the fact that the funds managed by Shri Arora had substantial stake in DGL (4.45% of the capital of DGL), the comment regarding the prospects of DGL cannot fall in the same category as a comment on trends in the securities market or on the economy. Thus he made a misleading statement with a view to affect the market price of DGL and thereby violated the provisions of Regulation 5 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 1995. The said Regulation 5 provides that

“No person shall make any statement, or disseminate any information which –

- (a) is misleading in a material particular ; and
- (b) is likely to induce the sale or purchase of securities by any other person or is likely to have the effect of increasing or depressing the market price of securities, if when he makes the statement or disseminates the information –
  - (i) he does not care whether the statement or information is true or false ; or
  - (ii) he knows, or ought reasonably to have known that the statement or information is misleading in any material particular ;

(2) Nothing in this sub-regulation shall apply to any general comments made in good faith in regard to –

(a) the economic policy of the Government,

(b) the economic situation in the country,

(c) trends in the securities markets, or

(d) any other matter of a similar nature,

whether such comments be made in public or in private.”

8.45 Having regard to the trading pattern elaborated above and the statement of Shri Arora made by him during an interview with Business Standard, I have no doubt in my mind that Shri Arora has violated Regulations 4(a), 4(b), 4(c), 4(d) and 5 of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995.

**Third issue :**

9.1 Whether Shri Samir C Arora is guilty of violating the provisions of Regulation 3 of SEBI (Prohibition of Insider Trading) Regulations 1992?

9.2 It is observed that there were no transactions in the scrip of Digital by the funds under Shri Arora’s management for quite some time i.e. from April 11, 2003 to May 7, 2003 but he suddenly became very aggressive in disposing off the entire holdings of 14.66 lakhs shares held by the funds under his management in 4 consecutive trading days commencing from May 8, 2003. The fact that the funds managed by Shri Arora did begin selling the shares of DGL which were held by them suddenly and inexplicably after a gap of about one month compared to the earlier transaction in the scrip and immediately after the submission of the valuation report by BSM does raise queries regarding what prompted Shri Arora to offload these shares. The reply of Shri Arora does not address this issue.

9.3 The Board of DGL at its meeting on May 12, 2003 was scheduled to discuss the merger ratio. The argument of Shri Arora that the ratio was not announced after the said Board meeting does not have any relevance. In fact, while making the

- sale on May 9, 2003 Shri Arora would have expected the Board of DGL to make the announcement regarding the merger ratio after the conclusion of the meeting on May 12, 2003. This explains the hurry shown by Shri Arora to dispose off the holdings before the conclusion of the Board meeting of DGL scheduled to be held on May 12, 2003.
- 9.4 If the reference to “tomorrow’s announcement” was indeed a reference to the financial results of DGL, I do not find any material to suggest that Shri Arora or the market expected adverse financial results. Thus, I find that the reason now being offered by Shri Arora does not explain what prompted him to sell the shares of DGL on May 9, 2003 and hence, is not acceptable.
- 9.5 That the merger ratio was not disclosed on May 12, 2003 at the conclusion of the board meeting of DGL, was not a decision planned for the meeting. Apparently during the course of discussions during the meeting on May 12, 2003 the Board of DGL did not reach a conclusion regarding the merger ratio and accordingly no announcement was made at the end of the meeting. Nobody including Shri Arora could have foreseen such development.
- 9.6 In his self-appraisal report, Shri Bhaskar Lakshminarayan has specifically mentioned that he had regular management meetings with two companies including DGL. In the said self-appraisal report for the period November 2000 to October 2001, Shri Bhaskar Lakshminarayan has himself mentioned that he already had 18 stocks under coverage and had added six more stocks during the year. The fact that he has identified only two stocks (viz. Digital and Hughes) out of the 24 covered by him, shows that his management meetings with DGL were not routine meeting.
- 9.7 On the one hand Shri Arora has stated that the funds managed by him were the second largest shareholder of Digital after Compaq is a ‘fact’ and on the other

hand he has insinuated that it is not proven by SEBI. I also note that he has not disputed what he himself has called a ‘fact’.

9.8 Notwithstanding the above, I note that the funds managed by Shri Arora were the single largest shareholder group of DGL after Compaq Computer Holdings Ltd. I find that the funds managed by Shri Arora were holding nearly 10% of the total paid up equity capital of DGL for several months and therefore it follows that ACM had a special interest in DGL and vice versa.

9.9 SEBI in its SCN has not stated that ‘anybody could compute the merger ratio’. In this regard, I note that SEBI has cited the statement of BSM that ‘if the assumptions and other variable factors in the valuation exercise are similar, the variation should not be significant if two separate audit firms value the companies.’ Shri Arora, in his above reply, has conveniently ignored the fact that, as per the statement of BSM, the merger ratio could be computed if the assumptions and other variable factors in the valuation exercise are known. Since SEBI has not stated that anybody could compute the merger ratio, the above reply of Shri Arora does not address any charge of SEBI. Also, the reply of Shri Arora ignores that BSM has stated to SEBI that ‘it had not made any changes in the information / projections submitted to DGL or HPI.’

9.10 In order to determine as to whether information relating to merger of DGL with HPI was price sensitive information or not, it might be appropriate to have a look at the definition of ‘Price Sensitive Information’ as given in Regulation 2(ha), which read as under:

“Price sensitive information means any information which relates directly or indirectly to a company and which if published is likely to materially affect the price of securities of company;

Explanation:-

- (i) periodical financial results of the company;
- (ii) intended declaration of dividend (both interim and final);

- (iii) issue of securities or buy-back of securities;
- (iv) any major expansion plans or execution of new projects;
- (v) amalgamation, mergers or takeovers;
- (vi) disposal of the whole or substantial part of the undertaking;
- (vii) any significant changes in policies, plan or operations of the company;”

9.11 I find that on June 9, 2003 (i.e. the trading day following the announcement of merger ratio on June 7, 2003), the scrip of DGL fell from Rs.500.5 to Rs.371.1 denoting a 26% fall. Thus, there is no doubt that the information regarding merger ratio was indeed price sensitive. SEBI has not charged Shri Arora that he received unpublished price sensitive information relating to DGL from Shri Hemant Soonawala. Hence, the issue of whether there was any interaction between Shri Soonawala and Shri Arora is not relevant.

9.12 Shri Arora has audaciously claimed that SEBI has twisted the interpretation of the term contained in one of SEBI’s own regulations. There is nothing in the SCN to suggest that SEBI has interpreted the term ‘person deemed to be connected person’ as contained in Regulations 2(h) of Insider Trading Regulations to suggest that any market intermediary could be a person connected with any other person in India.

9.13 I agree that Shri Arora was not personally registered with SEBI as an intermediary under Sec. 12. However, his claim of not being an employee of ACAML (which is an intermediary) is not tenable for reasons cited herein before.

9.14 Regulation 2(e) of SEBI (Prohibition of Insider Trading) Regulations 1992, states that “Insider means any person who, is or was connected with the company or is deemed to have been connected with the company, and who is reasonably expected to have access, to unpublished price sensitive information in respect of securities of a company, or who has received or has had access to such unpublished price sensitive information.” Regulation 2(h) of SEBI (Prohibition of

Insider Trading) Regulations 1992, inter alia provides that a person is deemed to be a connected person if such person is an intermediary as specified in Section 12 of the Act, Investment company, Trustee Company, Asset Management Company or an employee or director thereof or an official of stock exchange or of clearing house or corporation. Shri Samir C Arora is therefore an insider in terms of the above regulations.

- 9.15 It is not material whether Shri Arora was providing any service to DGL. The factual position was that the entities managed by Shri Arora, at some time or other, held as much as 10% of the paid up capital of the equity capital of DGL which holding was next only that of the controlling holder viz. Compaq. He and his analysts were maintaining constant and close interaction with the management of DGL. I find that Arora was indeed an Insider within the meaning of Insider Trading Regulations .
- 9.16 The sequence of events narrated in the SCN dated Feb. 20, 2004 clearly shows that Shri Arora was in possession of unpublished price sensitive information relating to the proposed merger of HP-ISO division with DGL and he has dealt in the scrip of DGL while in possession of the unpublished price sensitive information. As shown in an earlier paragraph, the said information was indeed price sensitive.
- 9.17 I find that since Shri Arora would indeed come within the ambit of an 'insider' as defined in Regulation 2(e) and 2(h) (ii) of SEBI (Prohibition of Insider Trading) Regulations, 1992, the requirement for SEBI to show that any other Insider has shared unpublished price sensitive information with Shri Arora does not arise.
- 9.18 I note that investigations have revealed violations of numerous provisions of SEBI Act, Rules and Regulations made thereunder by Shri Arora. With a view to protect the interests of investors and in order to promote orderly development of the securities market, SEBI has issued suitable directions as deemed appropriate

under Sections 11(4) and 11 B of the SEBI Act. No such actions have been taken against the other persons cited by Shri Arora since, as on date, SEBI has not found any evidence against those persons. In any case, if any person is found to have communicated un-published price sensitive information relating to the merger of DGL, SEBI shall take suitable action as deemed appropriate under the SEBI Act, Rules and Regulations made thereunder. Shri Arora himself has in his reply admitted that there is no case to proceed against BSM, any members of the board of directors of Digital or even the sub-committee of independent directors or the senior management of Digital. Hence, Shri Arora's contention that there is no whisper of any proceedings against these persons does not sound well.

- 9.19 As noted earlier Shri Arora was an Insider with respect to DGL, I note that the circumstances narrated in the SCN adequately show that Shri Arora has indeed dealt in the scrip of DGL on the basis of un-published price sensitive information. As per Regulation 2(e) of the SEBI (Prohibition of Insider Trading) Regulations 1992, an 'insider' means any person who, is or was connected with the company or is deemed to have been connected with the company, and who is reasonably expected to have access to unpublished price sensitive information in respect of securities of a company, or who has received or has had access to such unpublished price sensitive information. I view of this, I find that Shri Arora has indeed violated Regulations 3 of Insider Trading Regulations.
- 9.20 The denial of Shri Som Mittal and Shri Tendulkar of Digital that they had any interaction with Shri Arora during 2003 is not relevant since as noted earlier Shri Arora is an Insider with respect to DGL and has dealt in the scrip while in possession of unpublished price sensitive information. This aspect is fairly borne out of preponderance of circumstantial evidence available in this case.
- 9.21 The issue of Alliance Capital having sold 17.00 lakhs shares of DGL during the past six months has no relevance whatsoever to the charge of Insider Trading against Shri Arora and is an obvious attempt by Shri Arora to divert attention

- from the charges against him. I find it unnecessary to examine the motive of any person who may or may not have shared the unpublished price sensitive information with Shri Arora.
- 9.22 Circumstances narrated in the SCN clearly show that Shri Arora has dealt in the scrip of DGL during May 8-13, 2003 based on unpublished price sensitive information. The same is not a sweeping assumption as now being contended by Shri Arora.
- 9.23 The reasons now being cited by Shri Arora for his having sold the shares of DGL on May 9, 2003 do not appear in the rationale, recorded by Shri Arora, while selling the shares of DGL. These contentions of Shri Arora appear to be mere afterthoughts. Hence, I do not find any merit in the above contentions of Shri Arora.
- 9.24 The contentions of Shri Arora in his written submissions dated Aug. 27, 2003 have been suitably dealt with in SEBI's order dated September 24, 2003. Therefore, I do not find any merit in the assertion of Shri Arora that the SCN of SEBI does not deal with his contentions contained in his written submissions dated Aug. 27, 2003.
- 9.25 I note that any fund manager is required to record the rationale for each and every purchase and sale decision made by him. (Accordingly, Shri Arora has also recorded the rationale for the sale made by him in the scrip of DGL). At the point in time when Shri Arora had recorded the rationale for selling the shares of DGL on May 8-13, 2003, obviously he would not have imagined the likely repercussions. This could explain the reason for his faithful recording the rationale behind the sale of DGL scrip during May 8-13, 2003.
- 9.26 There is no convolution in the logic of SEBI as contended by Shri Arora. It is common for a fund manager to receive better remuneration if the funds managed

by him performed better. I also note that Shri Arora has not refuted this charge of SEBI.

9.27 Shri Arora has not contended that while he dealt in the scrip of DGL during May 8 -13, 2003 he had intended to resign from Alliance Capital. It is clear that at that point in time he had every intention to continue with Alliance Capital and reap the benefits of his actions through bonus. The contention that Shri Arora resigned from Alliance Capital without waiting to get the bonus does not lead to any inference relating to the personal benefits that were due to accrue to him. It is noted that following the SEBI's interim order dated August 9, 2003 Shri Arora was suspended by Alliance Capital from research and portfolio management and that his employment was to come to an end by September 2003.

9.28 In connection with the contention of Shri Samir C Arora that he sold the shares in DGL based on analyst's report and not based on any unpublished price sensitive information, it may be pertinent to advert to following events:

- Pursuant to the merger of Hewlett Packard and Compaq Worldwide, the process of de-merger of ISO division of Hewlett Packard India (HPI) with DGL, was initiated in October 2002. The impending de-merger was known to the market since that date.
- The DGL board appointed a committee of independent directors in April 2003 to finalize the de-merger issue.
- DGL appointed Bansi S Mehta & Co., Chartered Accountants (BSM) on May 2, 2003 to suggest a de-merger ratio. DGL had informal discussions with BSM on the valuation issue prior to the assignment given through a letter. BSM had several previous assignments with DGL in the past. The appointment was more of informal in nature.

- Shri Som Mittal, President and CEO of DGL met Shri Bansi S Mehta before the assignment was given and thereafter had regular discussions on the projections and estimates of the company.
- BSM completed the valuation and arrived at the merger ratio in a matter of 3-4 days. The main interactions were with DGL only. BSM did not make any changes but relied upon the projections and estimates made by DGL for the purpose of arriving at the merger ratio. BSM computed the valuation as per the Supreme Court case in Hindustan Lever as had been their practice. Given the data and other information, any other audit firm would have arrived at a similar ratio.
- On May 5, 2003, Shri Arora in an interview given to Business Standard talked positively about the DGL scrip. Particularly, he mentioned that the proposed merger is going to immensely help DGL due to the additional projects it is going to get from HP.
- On May 7, 2003, BSM submitted the de-merger ratio to DGL.
- On May 8, 2003 the following reports appeared in Economic Times “Digital Globalsoft, the 51% Indian software subsidiary of the Technology giant, Hewlett Packard (HP), vaulted 9.9% at Rs.609 following talks of a consolidation with Hewlett Packard Indian Software Operation (HPISO), 100% subsidiary of HP. Market Players expect the company to report a more than 50% jump in the profit for the quarter ended March 2003 of Rs. 38-40 crores. Speculation is also rife with regard to the new \$ 3 billion order received by HP worldwide from the US-based consumer major Procter & Gamble. Market players expect Digital Globalsoft’s volume to benefit from the order, though the exact nature of the benefit could not be ascertained. The company may announce a dividend of Rs.30-40 per share. It had cash per share of Rs.50 as on March 2002. It is likely to grow to Rs.70 per share.”

- On May 8, 2003, ACMF sold 119,000 shares of DGL while ACM sold 2,18,400 shares of DGL. The reasons as noted by Shri Samir C. Arora when he took the decision to sell the DGL shares “Price has rallied nicely – taking profits”
- With reference to the news article appeared on May 8, 2003, BSE issued a news release dated May 9, 2003 stating that the company has informed that following global merger between Hewlett Packard and Compaq, the future business and operating structure of Digital Globalsoft is currently under consideration. However, no decision in this regard has been arrived at. Until such time that a conclusive decision is taken, the Digital Globalsoft Board has officially indicated that the company’s business will continue as usual.
- On May 9, 2003 ACMF sold 334,562 DGL shares while ACM sold 250,000 DGL shares. The reasons as noted by Shri Samir C. Arora when he took the decision to sell the DGL shares - “Event risk in Digital is too high – getting nervous. Reducing exposure”
- On May 11, 2003 the Hindu Businessline inter-alia, reported that “The Digital May futures topped the list with active trading ahead of the company’s Q4 financial performance announcement on Monday.”
- The merger ratio was scheduled to be discussed / approved at the board meeting scheduled to be held on May 12, 2003 in which the financial results for financial year 2002-2003 was also to be finalized.
- DGL did not inform the stock exchange about the agenda of de-merger matter.
- On May 12, 2003 the results for the quarter ended March 2003 were approved by the DGL board in its meeting held at USA. The board accepted the valuation submitted by BSM. However, no final decision was taken.

- On May 12, 2003 ACMF sold 334,562 DGL shares while ACM sold 250,000 DGL shares. The reasons as noted by Shri Samir C. Arora when he took the decision to sell the DGL shares “Event risk from tomorrow’s announcements/results is too high. Bipolar situation but we do not like to take such risks post very high volatility in technology stocks around results/corporate issues.”
- The results of DGL meeting were known to the market on May 13, 2003 which was very much in line with the market expectations.
- May 13, 2003 at 9:17:22 AM - The corporate announcement as per BSE news release -“Digital Globalsoft announces Q4 & FY-03 results”
- On May 13, 2003 ACM sold 211,478 DGL shares.
- On May 30, 2003 DGL appointed Deolitte Haskins Sells (DHS) for a fairness opinion. DHS also affirmed the fairness of the de-merger ratio recommended by BSM.
- DGL Company announced the de-merger ratio on June 7, 2003. The ratio was perceived as unfavourable by the investors of DGL as well as by Shri Arora. The market fell by about 26% on June 7, 2003.

9.29 From the aforesaid sequence of events, it is clear that the market information did not indicate any adverse factor which could have prompted Shri Samir C. Arora to off-load 14,66,140 shares in four consecutive trading days starting from May 8, 2003. It is observed that there was increase in price from the closing price of Rs.537.55 on May 2, 2003 to Rs.597.25 at the close of business on May 7, 2003; an increase of 11.12%.

9.30 Thus the reason for the sale of shares, as noted by Shri Samir C. Arora could have been only “Event Risk in Digital is too high- getting nervous” and “Event Risk from tomorrow’s announcements’. The said event risks from tomorrow’s announcement was known to Shri Samir C. Arora but not known to the market. What could be these event risks from tomorrow’s announcement (i.e. May 12,

2003)? It definitely cannot be the favourable Q4 & FY-03 results of DGL. In this context it will be pertinent to advert to the following facts which came to light during the investigations viz.

- That Shri Som Mittal knew Shri Samir C. Arora for the past 5-6 years. Shri Samir C. Arora and his analyst used to make regular visits and interaction with the management and senior officials and discuss the performance and future plans of the companies in which they invest. It is also observed that Shri Bhaskar Laxminarayan who has been tracking DGL for several years and 'maintaining up-to-date files and having regular management meetings with DGL' purportedly sent an email to Shri Samir C Arora recommending to reduce position in DGL. The message inter alia mentioned 'valuation are capped unless ..... unexpectedly favorable scenario'.
- Shri Samir Arora, was solely taking all investment decisions of the equity and balanced funds of ACMF and the Indian allocation of ACM and their FII and sub-accounts. The funds held 14,66,140 shares of DGL which constituted about 4.45% of the total paid up capital of DGL. The fund had been holding the said shares since February 2001.
- The funds managed by Shri Arora was the single largest shareholder group of DGL after Compaq Computer Holdings Ltd. The funds were holding nearly 10% of the total paid up equity capital of DGL for several months (from January 2002 to January 2003) and therefore ACM had a special interest in DGL and vice versa.
- The coincidence of dates of submission of report by BSM to DGL and the sudden start of offloading of shares (which were held for past 2 years) by Shri Samir C Arora and the completion of offloading of all the shares of DGL in four consecutive trading days starting from May 8, 2003 to 13 May, 2003 i.e. the day on which the outcome of the Board meeting of DGL held on May 12, 2003 at San Francisco in USA, became public in India.

9.31 The aforesaid circumstantial evidences are predominant enough to indicate that, Shri Samir C Arora as an insider sold the shares of DGL while in possession of unpublished price sensitive information, related to merger. In the preceding paras it has already been concluded that Shri Samir C. Arora was an insider within the meaning of Regulation 2(e) and 2(h) (ii) of SEBI (Prohibition of Insider Trading) Regulations 1992.

9.32 Thus Shri Samir C Arora has violated Regulation 3 of SEBI (Prohibition of Insider Trading) Regulations 1992 and is guilty of insider trading as specified in Regulation 4 of SEBI (Prohibition of Insider Trading) Regulations 1992.

9.33 I have noted that adjudication proceedings have already been initiated against ACAML and ACM and therefore the contention of Shri Samir C. Arora that he has been singled out does not stand.

#### Cross examination

10.1 Shri Samir C Arora in his written reply dated 09.03.2004 to the show cause notice has sought for the cross examination of persons whose statements are relied upon by SEBI. However, during the oral hearing held on 24.3.2004, he did not raise this issue. I presume that he has realized the irrelevance of his request. The right of cross examination varies from case to case. It is settled principle of law that where prejudice is caused to the party by way of denial of facility for cross-examination by the authority, the same will be in breach of principles of natural justice. If the statements referred to in the show cause notice are the only evidence to come to an adverse conclusion against the noticee, the request for cross examination need to be accepted. In this case, I am of the view that sufficient evidence is available in the form of trading data, etc other than personal statements, for reaching the findings made hereinabove. Therefore, no prejudice is

caused to Shri Samir C Arora and no right of cross examination exists in the facts and circumstances of this case.

Inspection of unrelated documents

- 11.1 Further I have noted that Shri Samir C Arora, through his advocates and solicitors letter dated 11.03.2004 sought for inspection of documents in respect of other proceedings, if any, under way in SEBI, against ACMF, in so far they relate to Shri Arora, and also for copies thereof. He, however, did not raise this issue during the hearing. In this regard I find that SEBI had already given all the documents relied upon by it in support of the Show Cause Notice dated 20.02.2004. The proceedings against ACMF and others are independent of the proceedings taken against Shri Samir C. Arora and therefore have no relevance to the Show Cause Notice dated 20.02.2004 against him. I, therefore, find that there is no need, nor is it fair to give copies of the proceedings / documents as sought by Shri Samir C. Arora, in his letter dated 11.03.2004.

**CONCLUSION:**

- 12.1 From the aforesaid discussion I find that Shri Samir C Arora is guilty of grave professional misconduct calling for remedial action from SEBI under Section 11(4) and 11B of the SEBI Act. Shri Arora has also indulged in manipulative transactions and insider trading, thereby violated Regulation 4(a), 4(b), 4(c), 4(d) and 5 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations 2003 and Regulation 3 of SEBI (Prohibition of Insider Trading) Regulations, 1992.
- 12.2 It is to be noted that persons who operate in the market are required to maintain high standards of integrity, promptitude and fairness in the conduct of their business dealings. While “one is free to gain a competitive advantage in market place through conduct constituting skill, foresight, industry and the like”, no one

shall be let to gain undue advantage by unethical conduct, manipulation and privileged access to unpublished information and the like. It is the mandate of SEBI to protect the interest of investors and the safety and integrity of the securities market. If market participants/ intermediaries and more importantly even professionals commit serious violations, they ought to be dealt with severely by the Regulator, in the larger interest even on the basis of preponderance of evidence. The conduct of Shri Samir C. Arora was not in accordance with sound market principles. Considering the facts and circumstances of the case in totality and the blatant misconduct and violations committed by Shri Samir C. Arora of the regulatory provisions, I find it a fit case warranting serious action against him for his misdeeds so as to act as a deterrent for others of similar disposition.

- 12.3 Normally, action needs to be taken against the entity found guilty of violation of law. However, a corporate body operates and acts through its directors and other key persons in charge of its business operations. Corporate personality carries with it the discipline that those who avail themselves of the inherent privileges must abide by laws and regulations and adhere to the standards. A strong culture, positive or negative, will directly impact the control environment. Failure to take responsibility for the health of corporate culture can lead to apathy and a diet deficient of reinforcing procedures. It allows a malignancy to take hold and grow undetected. It may be, therefore, essential, in appropriate cases, to lift the corporate veil and take action against the individuals, whose conduct is primarily responsible for the misconduct or violation of law by corporate body besides action against the corporate body. Securities market is a very sensitive market and is prone to risks. Shri Samir C. Arora, the Fund Manager of ACMF who was a key functionary, is guilty of misconduct and violation of law as narrated hereinbefore and primarily responsible for the commissions and omissions of the Alliance Capital Mutual Fund and its AMC. Therefore, action against him is required in order to protect the interest of investors and ensure safety, integrity and the orderly development of securities market, besides action against the

Alliance Capital Mutual Fund and its AMC which SEBI has already initiated under the applicable rules and regulations.

## **ORDER**

13.1 In the light of the above and in exercise of the powers conferred on me in terms of Section 19 of the SEBI Act, 1992, read with Section 11(4) and 11B of SEBI Act, 1992, read with Regulation 11 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations 2003 and Regulation 11 of SEBI (Prohibition of Insider Trading) Regulations, 1992, I hereby prohibit Shri Samir C. Arora not to buy, sell or deal in securities, in any manner, directly or indirectly, for a period of five years. The period of prohibition already undergone by Shri Samir C Arora by virtue of the interim order dated August 9, 2003 will be included in the above period. However, if, in the meantime Shri Samir C. Arora desires to sell the securities, if any, currently held by him he may do so only after obtaining prior written permission of SEBI.

13.2 This order shall come into force with immediate effect.

**Place: Mumbai**  
**Date: MARCH 31, 2004**

**T M NAGARAJAN**  
**WHOLE-TIME MEMBER**  
**SECURITIES AND EXCHANGE BOARD OF INDIA**