

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

UNDER SECTIONS 11B AND 11(4) OF SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 IN THE MATTER OF
PENTAMEDIA GRAPHICS LTD.

WTM/GA/20/ISD/10/05

1.0. Background:

1.1. During the period March – May 2005, SEBI received complaints from Oriental Bank of Commerce, Mylapore Branch (erstwhile Mylapore Branch of the Global Trust Bank Ltd.) [hereinafter referred to as "OBC"], against Cameo Corporate Services Ltd., Chennai, (hereinafter referred to as "Cameo") Share Transfer Agents for Pentamedia Graphics Ltd. (hereinafter referred to as "PMGL"). In their complaints, OBC, inter alia, stated that they had sent to Cameo, share certificates for 34,00,000 equity shares of PMGL, held in the name of Vijay Advertising Private Limited (hereinafter referred to as "VAPL"), for transfer in the name of the Bank. OBC alleged that Cameo did not respond, despite repeated follow-up by OBC over a period of four months. OBC further informed that these shares were pledged in favour of the Bank as security for the huge dues payable by PMGL.

1.2. Further to the above complaint of OBC, SEBI sought certain clarifications from Cameo. In response, Cameo stated as under:

"As the distinctive nos. and certificate nos., comprised in the documents sent to us for transfer of 34 lacs shares did not match with the records maintained at our end, we could not effect the transfer of shares in the name of Oriental Bank of Commerce. In view of the above, we had, vide our letter dated 5.5.2005 returned the transfer documents to Oriental Bank of Commerce".

1.3. As the aforesaid reply given by Cameo raised doubts regarding the genuineness of the share certificates in question, SEBI advised Cameo to furnish certain additional information and the same were furnished by Cameo.

1.4. Further to the above SEBI obtained details relating to the major share holders of PMGL and the allotment of shares to VAPL by PMGL etc. from the depositories viz. National Securities Depository Ltd. (NSDL) and Central Depository Services (I) Ltd. (CDSL) and The Stock Exchange, Mumbai (BSE).

1.5. Based on the information obtained, the following facts emerged:

2.0. Facts of the Case:

2.1. PMGL is a listed company. Its shares are listed on BSE, NSE and Madras Stock Exchange (MSE). As on June 30, 2003, the paid up capital of PMGL consisted of 21,99,54,125 shares of Rs. 10/- each. PMGL has also issued GDRs with underlying equity shares.

2.2. On September 12, 2003, PMGL had issued 95,00,000 equity shares of Rs.10/- each on preferential basis at Rs.11.36 per share as approved by its Board of Directors. The details of the preferential allotment made to VAPL and Sathya Securities P Ltd. (hereinafter referred to as "SSPL") are as under:

Sl. No.	Name of the Allottee	No. of shares allotted	Rate	Amount (Rs. In Lakh)	% of Post Issue Capital of PMGL
1.	Sathya Securities P Ltd.	55,00,000	Rs.11.36	624.80	2.25%
2.	Vijay Advertising P Ltd.	40,00,000	Rs.11.36	454.40	1.63%

2.3. PMGL originally issued the certificates in physical form (printing of certificate done by PMGL directly) and sent the same to the allottees as above directly. PMGL vide its letter dated September 18, 2003 sent details regarding the above allotment / allottees to Cameo, for master updation. These shares were subject to lock-in up to September 11, 2004.

2.4. These shares, which were in physical form, were pledged by VAPL with OBC as security for the huge dues payable to OBC by PMGL.

2.5. Thereafter, while the physical shares were still under pledge to OBC, VAPL vide Demat Request Form No.3116548 dated July 17, 2004 sent another set of physical shares pertaining to the same distinctive number (as those pledged with OBC) to Cameo (the Registrar cum Share Transfer agent of PMGL) for dematerialization of the shares. The said demat request was sent by VAPL through IL&FS Ltd., a Depository Participant.

- 2.6. Cameo seems to have effected the dematerialization and uploaded the data in the normal course.
- 2.7. On December 30, 2004, OBC sent the original share certificates of PMGL lying with it as pledged along with Transfer Deed to Cameo with a request to transfer the shares (which were in the name of VAPL) to its name.
- 2.8. On receipt of the said request for transfer from OBC, Cameo noted that the physical shares sent by OBC had already been dematerialized by it (based on the earlier request by VAPL).
- 2.9. Cameo forwarded OBC's request along with the original documents to PMGL and sought PMGL's advice in the matter.
- 2.10. PMGL wrote to OBC offering to replace the share certificates pledged with OBC with some other shares for the same value.
- 2.11. Apparently, OBC did not agree and instead sent reminders to Cameo for effecting transfer. However, Cameo did not respond to OBC's letters till May 5, 2005. Cameo replied to OBC only after SEBI took up the matter with Cameo.
- 2.12. Cameo, vide its letter dated May 5, 2005 returned to OBC the original share certificates, along with other documents received by it stating that the distinctive numbers mentioned in the subject share certificates did not tally with its records.
- 2.13. From the aforesaid facts, it prima facie, appeared that there existed two sets of shares certificates of PMGL with the same distinctive numbers and hence at least one set had to be fake. In view of the above, SEBI vide an ex-parte interim order dated May 27, 2005, issued the following directions:

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1. **Pentamedia Graphics Ltd. and its directors** – PMGL is directed not to issue any further shares or alter its share capital in any manner till further directions. The company and its directors, namely Mr. V Chandrasekaran, Dr. S Ramani, Mr. T V Krishnamurthy, Ms. Usha Ganesarajah and Mr. S D Viswanathan are prohibited from accessing capital market or dealing in securities, in any manner, directly or indirectly, till further orders in this regard by SEBI.
2. **Vijay Advertising P Ltd. (Preferential Allottee)** – The sale proceeds accruing to VAPL from the above dubious deal is directed to be impounded and VAPL is further directed to retain the impounded sale proceeds in its account and the same should not be utilized in any manner for any purpose. VAPL and its directors namely Mr. M Vardharajan and Mrs. Bhuvaneshwari should not deal in securities market in any manner directly or indirectly till further directions by SEBI in this regard.”

OBC., Mylapore branch and Cameo were directed to preserve the original records available with them. An opportunity for post decisional hearing was granted to the aggrieved parties. PMGL, VAPL and their respective directors were granted 15 days time to file their objections to the ex-parte ad interim order.

3.0. Reply of PMGL:

- 3.1. PMGL vide letter dated June 6, 2005 and reiterated through letter dated June 9, 2005 enclosing supporting documents, inter alia, made the following submissions:

PMGL had various facilities from Global Trust Bank Limited (hereinafter referred to as "GTB"). The total outstanding as on 31st March 2005 payable to the OBC (in which Global Trust Bank Limited was merged) was Rs. 82.31 Crores. To settle the dues, PMGL arrived at an MOU with GTB in November 2003. The MOU envisaged the settlement of Rs.130 crores and also provided for payment of restructuring fee of Rs. 4 crores.

GTB insisted on marketable security to cover the value of the restructuring fee. Since the promoters of PMGL did not have any free shares, the company had requested VAPL to offer their shares acquired in preferential basis during September 2003 as an interim security to be offered to the bank till the promoters made alternate arrangements for the same.

In the meantime, VAPL had started pressing the company for release of the pledged shares and since there was an understanding that GTB was to return the shares for cancellation soon, PMGL issued shares to VAPL which had dealt with the same in the normal course. Subsequently, OBC lodged the shares for transfer in their name contrary to the understanding by the Company with GTB.

GTB has not informed the Registrar about pledge of shares with them by VAPL which clearly proves that it is only held for safety. Neither PMGL nor VAPL has derived any benefit by pledge of these shares. Issued subscribed & paid up capital has not gone up on account of the above, since demat request of OBC has been turned down by Registrar.

The company was settling the entire advance made by GTB which was unsecured and there was no compulsion for the company to indulge in such any wrongful act to defraud the bank for the sum of Rs.2.50 crores.

The company re-issued the shares to VAPL on a firm belief that GTB / OBC will return for cancellation the shares held by them. PMGL further stated that in the circumstances of the case, there being no fraudulent intention to either prejudice the interest

of investors or the Bank (OBC), Regulations 3 and 4(2)(h) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Markets) Regulations, 2003 are not attracted and thus no order under Section 11(B) and 11(4) are necessary. PMGL admitted that the bonafide actions of the company, does not result in the company being totally cleared of any mistake, negligence on its part and requested SEBI to take a lenient view as there was no intention for the company to sell the shares and make any profit and there was no malafide intention to defeat the rights of the Bank, prejudice the interest of the investors or take any action that may result in unfair trade practices in the securities market. In the light of the above submissions, PMGL requested that any unintentional and inadvertent procedural omissions on re-issue of shares be condoned and the proceedings be dropped.

4.0. Reply of VAPL:

4.1. Vide letter dated June 27, 2005, VAPL on behalf of the company and its Directors, namely Mr.M.Varadharajan and Mrs.Bhuvaneswari inter alia submitted as below:

4.2. It was pleaded that there was no mala fide or deceptive intention on the part of the Company in dealing with the shares of PMGL. Elaborating on the background of the transaction VAPL stated that VAPL was originally started as a Proprietorship in 1991 by name VIJAY ADVERTISING COMPANY and was involved primarily in advertising and other related activities. Its Sole Proprietor Mr. Vijay Bobby was a well established and experienced person in the Advertising Industry and was working in various capacities in the Advertising Field, viz., in Mudra Communication, Daily Thanthi ,etc. He had given a start and drive to the business and particularly focusing on the specialized field of advertising, namely Software Related Advertisements.

4.3.The Proprietorship firm promoted by Mr. Vijay Bobby had reputed clients in various fields, more particularly in software arena. The concern started thinking big and entertained ideas of entering into the segment of Internet Advertising and other related areas of business development. This involved an organized entity to be recognized by the customers and corporate and it was decided to convert the existing proprietorship into a Private Limited Company so that the benefits of the proprietorship could be enjoyed by the Company and hence in the year 1999, the Proprietorship was converted into a Private Limited Company. In order to effectively advertise Indian products in other countries through the media of internet advertising, the Company had approached PMGL in 2002 for using NUM TV.com, the web based entertainment portal as a base for advertisement. At that point of time, PMGL was one of the largest Indian Companies and was introducing internet based NUM TV.com in a big way through which they were telecasting various programmes in the USA and other western countries.

4.4.VAPL was one of the primary managers of PMGL's advertisement campaign in respect of this project and all other advertisements, assignments of various nature carried out by PMGL. In view of this, VAPL thought it fit that certain investments in PMGL would have synergies with their business plan and was able to understand the potential of the industry where internet based activity and keeping this in mind, made an investment of RS.454.40 lacs in PMGL for which 40 lacs shares were allotted at RS.11.36 per share on September 12, 2003 on preferential basis as approved by the Board of Directors and share holders of the company. But, in the meantime, the software boom started to recede and a slump in the whole industry saw many software companies closing down their operations resulting in a drastic reduction in the business of the Company thus shrinking their revenues.

4.5.However, VAPL, in view very strong business relationship with PMGL and also PMGL obliging the Company by giving a preferential allotment of the abovementioned shares, was always looking up to PMGL for its business development as it was the main source of revenue for the company. Hence, when PMGL started to have certain issues with banks, particularly, Global Trust Bank Limited, PMGL approached VAPL and requested for 34 lacs shares of PMGL, belonging to VAPL to be pledged with GTB temporarily and assured VAPL that it was only to enable them to bide time for providing alternate security. VAPL and its Directors had no option, in view of the company's business relationship, but to support PMGL at that juncture as sought for by them, even though VAPL had not borrowed any funds from Global Trust Bank. There is no prejudice that would be caused due to this as the shares were under lock-in and in any event VAPL was still prohibited from dealing with this stock and hence used this opportunity to enhance its goodwill with the management of PMGL. Accordingly they got the shares split and created pledge for 34 lacs shares on the condition that the return of shares should be as early as possible because VAPL also started running into financial constraints and should be in a position to raise funds by selling these shares as and when they were legally entitled to do so.

4.6.In the meantime, after the pledge had been created, there was no business forthcoming and also the business from software industry already touching a new low and pressure from market, liabilities started mounting and therefore VAPL insisted upon PMGL to return the shares pledged with Global Trust Bank Limited. There were no personal guarantees or any other guarantee provided by either VAPL or its Directors and hence when PMGL returned the shares in July 2004, VAPL sent them for dematerialisation in the normal course.

4.7.During September, when the lock-in period was over, to ease financial constraints, VAPL sold all the shares and settled its liabilities. The documentation done was only in regard to pledge and there being no security or other guarantees, VAPL was under the genuine impression that all its obligations have been relieved of and in fact as on date, there is no other obligation on its part in respect of the pledge. As a matter of fact, VAPL realised only Rs.169 lacs through sale of shares incurring

substantial loss in the process. Thus, there being no motives to make any profit. VAPL stated that its Directors are in no way connected with PMGL.

- 4.8. Cameo has, of its own accord, sent letters to SEBI explaining its roles and actions in this matter. I have perused the correspondence from Cameo. However, since there is no direction against Cameo, other than to preserve the original records, in the ex-parte ad interim order dated May 27, 2005, I consider that the same is not germane to the instant proceedings.

5.0 Oral Hearing:

- 5.1 Further, PMGL & directors appeared through Mr P.H. Arvind Pandian, Advocate on 16th June 2005 and filed written submissions vide his letters dated 23rd June 2005. PMGL made further submissions dated June 30, 2005 through its counsel reiterating the earlier submissions. Subsequently vide letter dated July 1, 2005, PMGL furnished a copy of the tripartite agreement dated March 9, 2004 for pledging third party securities entered into between GTB (the Bank), PMGL (borrower) and VAPL (guarantor).
- 5.2 VAPL and its directors failed to appear for post-decisional hearing on the appointed date as per the order dated 27th May 2005. Therefore, further opportunity was granted to them for personal hearing on 21st July 2005. During the personal hearing VAPL and its directors were represented by the same Advocate who appeared before SEBI on behalf of PMGL. Further VAPL filed written submissions vide letter dated 26th July 2005.

6.0 Findings:

- 6.1 I have carefully considered the oral and written submissions of PMGL, VAPL and its directors. My findings are as below:
- 6.2 PMGL had availed various facilities from GTB. For the purpose of settling its dues to GTB amounting to Rs.114.19 crores, PMGL had entered into an MOU dated December 29, 2003 with GTB. Upon perusal of the terms of MOU it is seen that PMGL was required to transfer title of various properties held by it and its subsidiaries, namely, M/s. Mayajaal Entertainment Ltd. and M/s Media Dreams Ltd. and also allot 3,00,00,000 (3 crores) equity shares (free of lock-in) of the company to the Bank and further make Rs.30 crores through 15 monthly instalments of Rs. 2 crores each and make various other payments over various periods. Further to the above restructuring of its dues, PMGL was required to pay GTB a restructuring fee of Rs. 4 crores. To secure the payment of restructuring fee, the bank stipulated that the promoters of the company shall pledge their holdings in PMGL or pledge the shares of any other listed company along with an irrevocable Power of Attorney authorizing the bank to sell the shares for realization of the amount of Rs. 4 crores. The MOU envisaged that the Bank and PMGL would jointly file the Consent Terms with Debt Recovery Tribunal (DRT) incorporating the provisions of the MOU and pray DRT to pass a decree in terms of Consent.
- 6.3 Since the promoters of PMGL did not have any free shares to be provided as security for the restructuring fee, the company had to arrange for third party pledge of shares. Accordingly, PMGL requested VAPL to offer shares of PMGL allotted to it on preferential basis during September 2003, as an interim security to be offered to the bank till the promoters made alternative arrangements for the same. PMGL has claimed that the shares of PMGL pledged by VAPL were to be kept by GTB only as security and not to be transferred. However, PMGL has not offered any document evidencing the above arrangement with GTB. VAPL had executed a tripartite arrangement with PMGL and GTB pledging the shares of PMGL held by it to GTB. GTB always had a right to enforce the pledge. Any putative arrangement to the contrary as canvassed by PMGL amounts to GTB extinguishing its right, which according to me, is opposed to all canons of banking practice. In the circumstances, the plea of PMGL is not only tenuous without any factual support, but also expects SEBI to set store on a weird concoction.
- 6.4 It actually turned out that OBC (erstwhile GTB) did approach the registrar viz. Cameo to get these shares transferred in its name. The offer of PMGL to OBC to replace the PMGL shares with some other shares for the same value also confirms the liability of PMGL to OBC. In view of this subsequent development as well, the version of PMGL that the shares offered as a pledge were to be treated only as security without transfer is further nailed to the counter.
- 6.5 In any case, the commercial exigencies and compulsions of PMGL does not justify PMGL to issue a second set of share certificates, bearing the same distinctive number as those pledged with the Bank. I note that PMGL has admitted to issuing another set of original certificate without cancelling the pre-existing certificates. I note that PMGL has attempted to downplay the gravity of the violation committed by it by claiming it to be an 'unintentional and inadvertent procedural omission on re-issue of shares. I do not agree that a serious violation such as knowingly issuing a fake share certificate can be regarded as unintentional procedural lapse in re-issue of shares. An act of fraud cannot be justified on such specious grounds which seek to make light of a venal act into one venial.
- 6.6 In this case, the consequences of the above action of PMGL are serious. While the allottee i.e. VAPL has illegally enriched itself through the sale of shares it was not rightfully entitled to, the bank is left with genuine share certificates which it finds unable to get transferred in its name to secure / recover its advances to the company. Considering the grave consequences of PMGL's actions, I do not agree with the contentions of PMGL that the violations committed by it are mere procedural omissions.

6.7 I find that VAPL had executed a tripartite agreement as a guarantor to secure the dues payable by PMGL to GTB. Pursuant to the tripartite agreement, VAPL had offered the lock-in shares held by it as pledge to GTB to secure the dues of PMGL. During July 2004, VAPL received the shares back from PMGL. VAPL in terms of prudent commercial sense should have insisted on a certificate from GTB discharging its liability. The fact that the share certificates were handed over to VAPL by PMGL without any covering letter from GTB / OBC should have raised the suspicion of VAPL regarding the genuineness of the certificates being returned to it. VAPL chose to overlook the suspicious circumstances in which the shares were returned to it, since VAPL is always seen to be as an adjunct to PMGL in the attendant circumstances of the case. Admittedly, VAPL had substantial business relationship with PMGL, which was amongst its major clients. PMGL had made preferential allotment to VAPL and VAPL offered these shares as pledge to secure the dues payable by PMGL to the bank.

6.8 A perusal of the audited annual report of VAPL shows that during the year 2002-03, VAPL had total income of Rs.22.36 lakhs and a net loss of Rs.3.55 lakhs. During the year 2003-04, VAPL had a total income of Rs.1.28 crores and a net loss of Rs.1.17 lakhs. As on March 31, 2004, VAPL had a networth of Rs.1.72 lakhs including accumulated loss of Rs.78,435/-. The Income Tax return filed by VAPL for the assessment year 2004-05 also shows a business loss of Rs.1.17 lakhs. In view of the small-scale of operations of VAPL and recurring losses, it was not clear how VAPL mobilized the Rs.454.40 lakhs, that it allegedly paid to PMGL towards subscription to the preferential allotment of 40,00,000 shares made during September 2003. In this regard, it is noticed that in the auditor's report annexed to the annual report of VAPL for the year 2003-04, it mentioned that "The company has availed loan from Malu Financial Services Ltd. to the extent of Rs.6,54,40,000/- during the year and have used the funds for subscribing to preferential issue of Equity shares of M/s. Pentasoft Technologies Ltd. and M/s Pentamedia Graphics Ltd. The loan amount is not due for repayment and no interest has been provided in the account while determining the profit or loss of the company." The rationale for a loss-making company with negligible networth i.e. VAPL borrowing crores of rupees to invest in shares that are subject to lock-in provision taxes one's credence and definitely requires further probe and SEBI has already ordered investigations into the matter. The whole sequence in a welter of related transactions, smacks of murky collusion between the players which is sought to be generously tweaked as a temporary business arrangement, when it was an elaborate edifice of public deception.

6.9 It appears that subsequent to the return of PMGL shares to VAPL during July 2004, VAPL has pledged these shares to one Gem Class P Ltd. and has raised a loan of Rs.97.50 lakhs, as could be gleaned from the enclosure to the letter dated 9th August 2005 from advocate to SEBI. Presumably this loan has been raised by VAPL to bail out PMGL. But definitely it does not support the version that VAPL sold the reissued shares at a loss to tide over its own financial difficulties.

6.10 In view of the close linkages between VAPL and PMGL, as narrated above, I am unable to convince myself that VAPL is an innocent party who acted in good faith while it dematerialized and sold the shares returned to it by PMGL. I hold that PMGL would not have gone to the extent of issuing fake shares unless it shared a relationship or cosy arrangement with VAPL. In the facts and circumstances of the case, it appears to me that there is interlacing and interlocking of intent between PMGL and VAPL and that their actions have resulted in a fraud being committed on the investors in securities market as well as the bank that had provided loans and advances to PMGL. For the purpose of issuing interim directions, I find that the evidence pointing towards the complicity of VAPL is preponderant enough to justify confirming the ad interim order with all the directions therein.

7.0 Conclusion:

7.1 In the light of the above, I find that, prima-facie, the conduct of the above entities is not in consonance with the high standards of integrity, fairness and professionalism expected from securities market participants. Such conduct by the said entities saps the investors' confidence and is detrimental to investor interests as well as the safety and integrity of the securities market.

7.2 Allowing PMGL, the preferential allottee viz. VAPL and their respective directors to continue their dealings in the securities market without any restrictions would be prejudicial to the interests of the investors and the safety and integrity of the securities market.

7.3 Issuing fake shares is a major offence. Fake shares will lead to artificial increase in shares of a company available for trading thus seriously impairing the value of securities held by genuine investors. Also fake shares will lead to artificial increase in trading volumes. Fake shares will also undermine the confidence of investors in securities market and seriously hinder the orderly development of securities market.

7.4 In the case of PMGL, the GDRs issued by the company are listed and traded in foreign countries. In case of such companies, it is all the more essential for companies to adhere to the highest standards of corporate governance in keeping with global benchmarks.

7.5 It is the responsibility of SEBI as market regulator to curb reprehensible practices such as issuing fake shares and trading in fake shares. Serious and deterrent penalties are called for to prevent recurrence of frauds such as issuing fake shares.

7.6 SEBI had initiated formal investigations into the matter. Based on the findings of investigation, appropriate proceedings will be initiated against the concerned entities as provided under the SEBI Act and the Rules and Regulations made thereunder.

7.7 In view of the seriousness of the acts committed by PMGL, VAPL and directors of these companies, I have no hesitation in confirming the ad interim order dated 27th May 2005, with all the directions mentioned therein, in the interest of the investors and safety and integrity of the securities market.

This order shall come into force with immediate effect.

Place: Mumbai

Date: 3rd October, 2005

**G ANANTHARAMAN
WHOLE-TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA**