

SECURITIES AND EXCHANGE BOARD OF INDIA

Coram: Dr. T. C. Nair, Whole Time Member

Name of the noticee: M/s. Kuku Motor Finance Limited and its Director,
Shri S. K. Chadha

Date of Hearing : 11-07-2006

Appearance of Parties

For the Noticees : None

For SEBI : Shri P. K. Bindlish, General Manager
Shri Ashok Nimbekar, Manager

DIRECTIONS UNDER SECTION 11(4) (b) READ WITH SECTION 11B OF THE SEBI ACT, 1992 AND REGULATION 11 OF SEBI (PROHIBITION OF FRAUDULENT AND UNFAIR TRADE PRACTICES RELATING TO SECURITIES MARKET) REGULATIONS, 1995 READ WITH REGULATION 13 OF SEBI (PROHIBITION OF FRAUDULENT AND UNFAIR TRADE PRACTICES RELATING TO SECURITIES MARKET) REGULATIONS, 2003 AGAINST M/s. KUKU MOTOR FINANCE LIMITED AND ITS MANAGING DIRECTOR SHRI S. K. CHADHA IN THE MATTER OF M/s. NATURAL EXPO AGRO INDUSTRIES LIMITED

WTM/TCN/ID3/04/4/2007

1.0 BACKGROUND

1.1 Natural Expo Agro Industries Ltd. (NEAL) is a public limited company with its registered and corporate office at 9th Floor, Galav Chambers, Near Sardar Patel Statue, Sayaji Gunj, Vadodara, Gujarat 390005. NEAL came out with a public issue of Rs. 275 Lakh in February-March, 1996, in order to part-finance the project for manufacturing Jaquard Woven Furnishing and Curtain Fabrics. The issue for 77 lakh equity shares of Rs.10/- each for cash aggregating to Rs.770 Lakh opened on 3.5.95 and closed on 6.5.95. Several complaints were received regarding delay in transfer of shares and manipulation of price of the shares. A preliminary investigation by the Securities and Exchange Board of India (hereinafter referred to as SEBI) showed that there was a delay in transfer of shares as well as in the dispatch of shares after transfer. It was also noted that trading in the share was suspended by the Bombay Stock Exchange Limited (BSE) on some days on account of abnormal increase in the price. In view of the above, investigation was ordered into the affairs relating to dealing in shares in respect of public issue by NEAL, its lead manager, Registrar and other persons/intermediaries associated with the public issue, vide order dated 30.1.97.

1.2 The report on investigation was submitted to SEBI on 18.4.2002. Investigations revealed that:

- a. NEAL did not receive the minimum required subscription to the public issue; it was subscribed only to the extent of 14%;
- b. In order to circumvent the requirement of minimum subscription, NEAL had entered into an arrangement through M/s. Galav Finance and Investments Pvt. Ltd. (GFIL) whereby they financed applications for the issue in order to ensure minimum subscription and NEAL purchased back the shares allotted. It was seen that NEAL transferred funds to GFIL which in turn transferred the funds to the applicants who later issued cheques to NEAL. Thus, NEAL did not receive any real consideration and also utilized the proceeds of the public issue for arranging subscription and for circumventing the requirement of minimum subscription;
- c. NEAL and its directors made allotments without receiving the minimum subscription in the Issue;
- d. The share certificates allotted to the applicants were not dispatched to them by NEAL. Rather these shares were retained by the company. 6 Lakh shares which had arrears of call money were traded in the market through various brokers including GFIL. The prices of the scrip went up abnormally due to the cornering of shares coupled with artificial scarcity of stock through intentional delay in transfer of shares

1.3 In the course of investigation, it was also noted that on BSE the opening price of the scrip was Rs.19 on 3.7.95 and went up to Rs.50 on 18.7.95. After being in the range of Rs.30 to Rs.50 till 1.9.95, the price fell to Rs.15 on 18.9.95. It was in the range of Rs.26 and Rs. 50 between 25.9.95 and 8.12.95. The opening price on 4.1.96 was Rs.48. Thereafter, the price of the scrip showed a rising trend and went up to Rs.88.75 on 20.2.96. It then showed a continuous downward trend to end at Rs.9.25 on 13.5.96.

1.4 On NSE, the opening price of the scrip was Rs.15.50 on 26.6.95; it went up to Rs.51 on 24.7.95. After being in the range of Rs.30 to Rs.46 till 31.8.95, the price fell to Rs.19.50 on 14.9.95. It moved in the range of Rs.25 and Rs. 51 between

25.9.95 and 22.12.95. The opening price on 2.1.96 was Rs.46. Thereafter, the price of the scrip showed a rising trend and went up to Rs.84 on 8.2.96. It then showed a continuous downward trend to end at Rs.11 on 15.5.96.

- 1.5 The investigations also brought out that M/s. Kuku Motor Finance Limited (KMFL) had acted as a lead manager to the issue thereby, being responsible for both pre and post issue activities. KMFL had failed to ensure that the allotments pursuant to the public issue of NEAL were made only after due receipt of the application money for the shares to be allotted. This resulted in a failure on the part of KMFL to comply with the Code of Conduct prescribed in Schedule III of SEBI (Merchant Bankers) Rules and Regulations, 1992. The compliance of Code of Conduct is mandatory as per Regulation 13 of SEBI (Merchant Bankers) Regulations, 1992.
- 1.6 KMFL was also alleged to have violated SEBI Circular No. PMD/CIR.217891/92 dated 24.12.92, which states that the Lead Manager responsible for post issue activities shall have a close co-ordination with the Registrars and arrange to depute its Officers at regular intervals after the closure of the issue to monitor the flow of applications from collecting branches, processing of applications including those accompanied by stock invests and other matters till the basis of allotment is decided, and to ensure that the despatch of Share Certificates and refund cheques are completed in time and listing of the shares is done in the designated Stock Exchange.
- 1.7 It was brought to light that KMFL was no longer a registered merchant banker with SEBI, which would render it liable for actions under SEBI (Procedure for Holding Inquiry by and Enquiry Officer and Imposing Penalty) Regulations, 2002. Therefore, SEBI initiated action under Section 11(4) and 11B against KMFL and its Managing Director, Shri S. K. Chadha in the matter.

2.0 SHOW CAUSE NOTICE, REPLY AND HEARING

- 2.1 A notice dated 21.07.04 was issued to KMFL and its Managing Director, Shri. S. K. Chadha, wherein it was stated that KMFL had violated Code of Conduct for Merchant Bankers and SEBI Circular No. PMD/CIR.217891/92 dated 24.12.92. The noticees were asked to show cause as to why appropriate directions including directions debarring KMFL and its director, from acting as an intermediary in the capital market, prohibiting access to the capital market and dealing in securities, should not be issued under Section 11B and 11 (4) of SEBI Act, 1992.
- 2.2 No reply to the show cause notice was received from KMFL and its director. Thereafter opportunities of hearing were granted by me to KMFL and its managing director on various occasions. The final such opportunity was given on 11.07.06. KMFL and its managing director failed to turn up for the hearing before me.

3.0 CONSIDERATIONS OF ISSUES

- 3.1 I have considered the findings of the investigations, the charges made out in the show cause notice dated 21.07.04 against KMFL and its managing director. I find that KMFL and its managing director, Shri. S. K. Chadha had been given numerous opportunities to respond to the Show Cause Notice issued by SEBI and also to make their submissions during hearings scheduled from time to time and finally on 11.07.06. I have noticed that KMFL is under liquidation and letters issued by SEBI have been served to the company and its managing director based on the last available address with the Official Liquidator of KMFL. This, I feel, is sufficient compliance of the principles of natural justice with regard to KMFL and its managing director. Further opportunities to KMFL and its managing director would only lead to delay in the completion of the proceedings in the scrip of NEAL by SEBI. Therefore, I proceed to examine the charges against KMFL and its managing director Shri. S. K. Chadha, on merit.
- 3.2 I have seen that SEBI has passed orders against various delinquent entities in the scrip of NEAL, including NEAL and its directors for the violations committed by them during the public issue of NEAL and the subsequent price manipulation in the scrip. I have also noted that the orders against NEAL and its directors have not been appealed against thereby becoming binding on them. This goes to prove the allegations in respect of the public issue made against NEAL. As has been brought out by the investigation, the issue did not elicit the minimum subscription of 90% as has been prescribed under the Companies Act, 1956, for successful completion of an issue. Consequently, NEAL had made fictitious arrangements for ensuring the minimum subscription of the public issue to enable the allotment of shares therein.
- 3.3 For this purpose, NEAL had entered into financing arrangement through Galav Investments and Finance Ltd. (GIFL) with six applicants to the issue. The shares allotted to these six entities were never delivered to the entities and was used by NEAL to influence the price in its scrip and ultimately to sell the same at a profit. It was noted that 435 applications were received for 69,76,800 shares and according to which, the issue was subscribed to the extent of 90.61%. From the list of applicants and allottees, it was noted that the following six applicants had applied for and had been allotted 60 lakh shares i.e. approx. 86% of the total shares allotted in the issue.

Applicant	Stock invest No.	Issued By	Shares	
			Applied	Allotted

Ketan Doshi Toophanmal Bhandari	12068	Global Trust Bank	100000	100000
Piyush Avlani Toophanmal Bhandari	12065	Global Trust Bank	100000	100000
Bhavna K. Doshi Toophanmal Bhandari	12064	Global Trust Bank	100000	100000
Kamlesh Doshi Toophanmal Bhandari	12066	Global Trust Bank	100000	100000
Muktaben H. Doshi Toophanmal Bhandari	12063	Global Trust Bank	100000	100000
Paulomi Doshi Toophanmal Bhandari	12067	Global Trust Bank	100000	100000

All the applicants mentioned above had shown their address as Nirmal, 3rd Floor, Nariman Point, Mumbai – 21. Investigations revealed that the above address was that of one DCW Finance Ltd. (DCW) and one Shri Toophanmal Bhandari, the second applicant in all of the above applications was the Vice President of DCW. It is also noted that the share certificates were not handed over to the above allottees and the same were returned back to NEAL.

Further, it was observed from the extract of the current account statement of NEAL and GFIL maintained with Union Bank of India, Nariman Point Branch, that the flow of funds was as under:

Date	Particulars	Amounts credited/debited in the accounts of (in Rs.)		
		NEAL	GFIL	NEAL
3.6.95	From NEAL to GFIL	3005000		
3.6.95	From GFILto Ketan Doshi		3005000	
5.6.95	From NEAL to GFIL	1400000		
6.6.95	From GFILto Ketan Doshi		1400000	
8.6.95	From Ketan Doshi to NEAL			5000000
9.6.95	From NEAL to GFIL	5000000		
13.6.95	From GFILTo Piyus Avlani		5000000	
15.6.95	From Piyush Avlani to NEAL			5000000
16.6.95	From NEAL to GFIL	5000000		
16.6.95	From GFILto Paulomi Doshi		5000000	
20.6.95	From Paulomi Doshi to NEAL			5000000
21.6.95	From NEAL to GFIL	5000000		
21.6.95	From GFILto Bhavna Doshi		5000000	
22.6.95	From Bhavna Doshi to NEAL			5000000
23.6.95	From NEAL to GFIL	5000000		
23.6.95	From GFILto Muktaben Doshi		5000000	
27.6.95	From Muktaben Doshi to NEAL			5000000
28.6.95	From NEAL to GFIL	2500000		
28.6.95	From GFILto Kamlesh Doshi		2500000	
29.6.95	From Kamlesh Doshi to NEAL			2500000
4.7.95	From NEAL to GFIL	2500000		
4.7.95	From GFILto Kamlesh Doshi		2500000	
5.7.95	From Kamlesh Doshi to NEAL			2500000
		29405000	29405000	30000000

From the above, I note that NEAL had credited amounts to GFIL on various dates and these amounts were then credited by GFIL to the respective applicants on the same day. Thereafter, the same amounts were credited to NEAL by the applicants. It is further noted that the amounts were transferred from NEAL to the applicants through GFIL after finalization of allotment on 27.5.95 i.e. after NEAL informed DCW that the stock invests were lost and advised them to submit cheques for the amounts. Further, as per details provided by NEAL only a sum of Rs.38,15,500/- has been collected on account of Call Money. This implies that only 7,63,100 shares out of 69,76,800 shares were fully paid up and the remaining were partly paid up. Thus, no consideration was actually received by NEAL for the shares allotted to the six applicants and that the amounts were provided to the applicants to give an impression that the loss of stock invests of value Rs.300 lakhs had been

fully made up and the issue had been subscribed. If the said applications are not taken into account, the issue would have been subscribed only to the extent of 14%.

- 3.4 KMFL as the Lead Manager to the issue was responsible for the pre and post issue activities. By virtue of the said responsibility, KMFL had to co-ordinate with the Registrars for proper completion of the issue and allotment of the same. It has been submitted by NEAL that the stock invests submitted by the six entities had been lost subsequent to the finalisation of the basis of allotment and therefore, these entities were asked to submit cheques for equivalent amount. But, the moneys to be paid by these entities were actually routed from NEAL through GIFL out of the public issue proceeds which NEAL had hitherto received. The bank account of GIFL with the Union Bank of India, Nariman Point Branch, Mumbai is a clear proof of the movement of funds to these six entities. Also, the investigations have brought out the full sequence of fund movement from the account of NEAL and back to the accounts of NEAL. KMFL has not exercised due care and diligence in processing the applications. As stated earlier, the six applications carried the same address which the lead manager failed to notice. Even though there is no bar of the number of applicants from the same address, the same should have cautioned KMFL and they should have taken abundant care and caution while processing the applications.
- 3.5 KMFL by not exercising care and diligence in processing the applications had thus violated SEBI Circular No. PMD/CIR.217891/92 dated 24.12.92, which states that the Lead Manager responsible for post issue activities shall maintain a close co-ordination with the Registrars and arrange to depute its Officers at regular intervals after the closure of the issue to monitor the flow of applications from collecting branches, processing of applications including those accompanied by stock invests and other matters till the basis of allotment is decided, and to ensure that the despatch of Share Certificates and refund cheques are completed in time and listing of the shares is done in the designated Stock Exchange. The Lead Manager has failed to detect any of these irregularities at the time of allotment and has not ensured that there is a complete compliance of the requirements in this regard. This enabled the public issue to sail through, resulting in 14% of the applicants being misled to believe that the issue had been properly or fully subscribed to and there was genuine market interest in the scrip of NEAL. The non-compliance to the above referred circular would constitute a blatant violation of the Code of Conduct prescribed for Merchant Bankers.
- 3.6 Therefore, in my view KMFL and its director, Shri S. K. Chadha are guilty of violating the provisions of the Code of Conduct for Merchant Bankers and the aforesaid circular. I note that SEBI has been empowered under Section 11 B and 11(4) of SEBI Act, 1992, to issue directions against the entities. Though Section 11(4) was not inserted in the SEBI Act at the time of the specified violations committed during February-March, 1996, it is my firm view that the power conferred under Section 11(4) of SEBI Act is none but an elucidation of the powers already available with SEBI under Section 11 of the SEBI Act, 1992. Therefore, it would be appropriate and justified in law to pass orders against KMFL and its director under Section 11B and Section 11(4) of SEBI Act, 1992.

4.0 ORDER

- 4.1 In view of the aforesaid findings, I, in exercise of powers conferred upon me in terms of section 19 of SEBI Act, 1992 read with Section 11B and 11(4) of SEBI Act, 1992, hereby direct that M/s. Kuku Motor Finance Limited and its Managing Director, Shri. S. K. Chadha be debarred from acting as an intermediary in the capital market and be prohibited from accessing the capital market and dealing in securities directly or indirectly for a period of six months.
- 4.2 The order shall come into force with immediate effect.

DATE: 26-04-2007
PLACE: MUMBAI

T. C. NAIR
WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF INDIA