

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA

CORAM: Dr. T.C.NAIR, WHOLE TIME MEMBER

AGAINST D- LINK (INDIA) LIMITED

Date of hearing : September 13, 2006

Appearances:

For Noticees : Shri Virag Tulzapurkar, Senior Advocate
Shri S.H. Bhojani, Advocate
Shri I.D. Deshmukh
Shri K.G. Prabhu, Company Secretary, D Link

For SEBI : Shri P.K.Bindlish, General Manager
Shri Pradip Bhowmick, Manager
Ms. Kshama Chavan, Legal Officer

ORDER

UNDER SECTION 11B & 11(4)(b) OF SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 READ WITH REGULATION 11 OF SEBI (PROHIBITION OF FRAUDULENT AND UNFAIR TRADE PRACTICES RELATING TO SECURITIES MARKET) REGULATIONS, 1995

1.0 Background

1.1 Securities and Exchange Board of India (hereinafter referred to as 'SEBI') observed a spurt in the price and volume in the scrip of D- Link (India) Limited (hereinafter referred to as "DIL") at the Bombay Stock Exchange Ltd. (hereinafter referred to as 'BSE') and the National Stock Exchange of India Ltd. (hereinafter referred to as 'NSE') during the period November 03, 2003 to December 03, 2003. At BSE, the price rose from Rs. 107.40 to Rs. 191 with

volume varying between 76,000 shares and 4.5 lakh shares. At NSE, the price rose from Rs 107.60 to Rs.189.60 with volume varying between 88,000 shares and 17 lakh shares.

- 1.2 Subsequently, SEBI received a complaint dated October 02, 2003 from an investor, Shri Ravi Deshmukh inter alia alleging that inspite of passing a special resolution authorizing the Board of Directors (BoD) of DIL to buy back its equity shares for an amount not exceeding Rs. 160 million, upto a maximum price of Rs. 80 per equity share, in the Extra-Ordinary General Meeting (EGM) convened on September 30, 2002, the company did not buy back those shares which resulted in loss to the small investors who had bought shares from open market in anticipation of the said buy back.
- 1.3 During the course of investigation, it was noticed that lot of news were emanating in the media relating to the corporate developments of DIL. Further, the BoD of DIL in its meeting held on August 09, 2002 passed a resolution authorizing the BoD to convene an EGM on September 30, 2002, [when Annual General Meeting (AGM) was already scheduled to be held on August 24, 2002] for amending the Articles of Association to insert a new clause on buy back of shares and to get the same approved by the shareholders.
- 1.4 Accordingly, on September 30, 2002, an EGM was convened to discuss the issue of buy-back. In the EGM, the shareholders authorized the Board to buy back such of company's own shares or securities as it may think necessary subject to such limit, upon such terms and conditions, and in accordance with the provisions of sections 77A, 77AA and 77B of the Companies Act. However, no further action, as per provisions of section 77A of the

companies Act, in this regard was taken by the company. It was observed that the share price at the time of EGM was around Rs.63 and thereafter it came down to Rs.41.55 on April 23, 2003. Subsequently, the price went to a high of Rs. 106.25 on October 1, 2003. Thus, small investors who had purchased the shares in anticipation of the buy back had to sell the shares at a loss since the buy back offer was never made.

- 1.5 It was alleged that the aforesaid acts of DIL construed as misleading information to the public and the company deliberately misled common investors by disseminating the news pertaining to buyback of shares.

2.0 Show Cause Notice

- 2.1 A show cause notice dated May 05, 2006, was issued to DIL and Shri K R Naik, Chairman and Managing Director of DIL, to show cause as why action should not be taken against them under section 11B & 11(4)(b) of the SEBI Act, 1992 read with Regulation 11 and 12 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices) Regulations, 1995 (hereinafter referred to as “PFUTP Regulations”) read with relevant provisions of SEBI (PFUTP) Regulations, 2003 for disseminating misleading information.

- 2.2 DIL vide letter dated June 15, 2006, replied to the aforesaid show cause notice and inter alia made submissions as under :

- (i) As regards, dissemination of information is concerned, DIL sent a notice of EGM and the intimation to the Stock Exchange was in bonafides, good faith and in compliance with relevant provisions of the Companies Act, 1956 and the listing agreement respectively. DIL was required by law to give information to its shareholders and stock exchange. DIL denied that it flashed a corporate announcement on the BSE website on October 04, 2002 and stated that it was not in control of or in a position to influence what appeared on the BSE website. It was sole discretion of BSE to decide regarding what appeared on its website. The company had merely sent notice of EGM to its shareholders and*

- intimation regarding the same to stock exchanges did not amount to “dissemination” as contemplated under PFUTP Regulations, 1995.
- (ii) *At the EGM, the shareholders of DIL passed a resolution authorizing the BoDs to buy-back the shares. The said special resolution did not impose an obligation on the Board to buy-back its shares. The notice of EGM revealed that the proposed resolution was meant inter alia only to empower and authorise the Board of Directors to buy-back, if they thought fit. Therefore the resolution only conferred a power of authority to the BoDs to buy back could be said to have been imposed an obligation on the Board of Directors of DIL to buy-back.*
 - (iii) *At the time of passing the special resolution, DIL intended to give an option and authority to the Board of Directors of DIL to decide whether or not to buy-back. It denied dissemination of any information which could be said to be misleading. If some speculator misinterpreted or speculated with a view to buying any shares so as to profit if a buy back was made, DIL cannot be held responsible. Further the authority given by special resolution to buy-back was upto a maximum price of Rs. 80/- per share and not at Rs. 80/- per share. The speculators were therefore not justified in expectation of a buy back price of Rs. 80/-.*
 - (iv) *Dissemination of information should have resulted in increase in demand for scrips of DIL leading to increase in its price. But on the contrary, the price of the scrips of DIL dramatically fell after October 4, 2002 which indicates and confirms that the investors at large and members of DIL were aware that the special resolution only grants authority to the Board of Directors of DIL to decide whether or not to buy-back and in any event does not reflect a final decision by DIL to buy-back.*
 - (v) *The facts contained in the notice of EGM and intimated to the stock exchanges were true and not misleading as alleged. DIL was bound in law to furnish the information to the Stock Exchanges.*
 - (vi) *Section 11(4)(b) was incorporated in the SEBI Act, by SEBI Amendment Act, 2002 and gained force only on October 29, 2002 and as alleged violations have admittedly taken place on or about October 4, 2002, no action can be taken against DIL under section 11(4)(b) of the SEBI Act. It is submitted that section 11(4)(b) of the SEBI Act is ex post facto law, its retrospective application to the present case will violate DIL’s fundamental right guaranteed under Article 14 of the Constitution of India.*

(vii) The complaint filed by Shri Ravi Deshmukh was unfounded and did not have any locus standi for filing such complaint as he was not a member/investor in DIL during the relevant period.

3.0 Personal Hearing

3.1 An opportunity of hearing was granted before me on September 13, 2006 wherein person stated on the first page of the order appeared before me and made submissions. Further written submissions were submitted by D Link vide letter dated September 21, 2006 which have been taken on record.

4.0 Consideration of Issues and findings

4.1 I have carefully considered the show cause notice issued to the noticees and the replies thereof. I observed that:

4.2 The decision to convene the EGM for the purpose of altering the Articles of Association of the company to insert a new clause on buyback of shares and to get the EGM's approval for the buyback was taken in the BoDs meeting of the company held on August 09, 2002, when the AGM of the company was already scheduled to be held on August 24, 2002. The notice of EGM dated August 9, 2002 at which the special resolution was proposed to be passed was sent to the shareholders. The special resolution was passed by the company on September 30, 2002 which was communicated to BSE. BSE uploaded this information on its website on October 04, 2002. The information about buy back of shares by the company is price sensitive information which may result in enhanced trading in the scrip of the company, as this act on the part of the company indicates the confidence of the management in the value of the share of the company. DIL in the special resolution stated that it proposed to buyback shares upto a maximum price

of Rs. 80 per share. The special resolution passed also gave full discretion to the BoDs to do all such acts, deeds, matters and things as may in its absolute discretion, deem necessary expedient.

- 4.3 In this regard, it is noted that quite contrary to the issue raised by DIL, exchange (s) upload information regarding any corporate development, etc., on their website as submitted by the concerned company. It is the responsibility of the concerned company to submit true/correct information to the exchange so that the shareholders and investors can take appropriate investment decisions.
- 4.4 The share price of DIL at the time of EGM was around Rs. 63 and thereafter it came down to Rs. 41.55 on April 23, 2003. Subsequently, the price went upto a high of Rs. 106.25 on October 01, 2003. I note that after the special resolution was passed, the market price had decreased and it never reached the maximum price that was announced i.e. Rs. 80, till August 03, 2003 i.e. until 10 months after the resolution was passed. From this I note that DIL had enough opportunities to implement the resolution of buy-back passed in the EGM as the price of the scrip was lower than the buy back price for most of the period during the currency of resolution.
- 4.5 As indicated by the company in its notice of EGM, the objective of buy-back was to 'increase the wealth of the shareholders'. However, I have observed that in the subsequent meetings of BoDs of DIL held on October 31, 2003, January 30, 2003, February 06, 2003, May 17, 2003 and July 31, 2003, there was total inaction in the matter of buy back. DIL had neither intimated the stock exchanges nor the share holders that the buyback was not being proceeded with. This meant that the company had no intention of implementing the

buyback even though their stated objective was to enhance shareholder's wealth as there were enough opportunities available to buy back the shares much below the maximum price proposed.

- 4.6 I note that DIL has taken the plea that buy back was subject to the discretion of the BoDs and the company was under no obligation to go in for the said buy back. The relevant part of the special resolution reads as under:

“Notwithstanding anything contained in these Articles, the Board of Directors may, when and if thought fit, buy back such of the company's own shares and securities as it may think necessary, subject to such limits, upon such terms and conditions, and in accordance with the provisions of Sections 77A, 77AA and 77B of the Act or any Statutory Modification thereto and such other regulations and guidelines as may be issued in this regard.

“RESOLVED FURTHER THAT *the Board of Directors of the company be and is hereby authorised to take all such actions and do all such things as may be necessary from time to time for giving effect to the above resolution and matters incidental thereto.”*

On perusal of the above, I have noticed that the special resolution passed at the EGM indicates that the final decision with respect to implementation of buy back vested with the BoDs. Agreeing to this fact, had DIL any intention to buyback its shares, it would have taken some measures in the interim period between passing special resolution and its validity period i.e. twelve months from the date of passing the special resolution in the general meeting. Also, I note that no information regarding implementation / withdrawal of the buyback of shares was sent to the shareholders / stock exchanges during the statutory period. Section 77A (4) of the Companies Act, 1956 says that *“Every buy-back shall be completed within twelve months from the date of passing the special resolution”*. From the chronology of events, I find that DIL had not initiated the buyback within a period of twelve months of

passing the special resolution in violation of section 77A (4) of the Companies Act, 1956. The contention of DIL that the special resolution did not impose an obligation on the BoDs to buy back the shares is therefore not acceptable.

4.7 Thus, I find that DIL's submission that *"the company had originally proposed to deploy only upto Rs. 16 crore in the event it decided to exercise the option to buy back. However in view of the increase in the company's expenditure on fixed assets and the eventual expenditure thereon in excess of Rs. 14.30 crore, it was not feasible for the company to consider the option of buy back during the relevant period"* holds no water. I note that as per section 217 (2B) of the Companies Act, 1956, the company who proposes to go for a buy back is required to specify the reasons for the failure, if any, to complete the buy back within a period of 12 months in its Board of Director's report. Though DIL while passing the special resolution in the EGM, intended to give an option and authority to the Board of Directors to decide whether or not to buy back the shares of the company, the non compliance of the same should have been reported to in the Board of Directors Report for the year 2003-2004. However after perusal of the Annual Report for the year 2003-04, I observe that the Annual Report does not indicate the reasons for not implementing the buy back or not giving effect to the special resolution.

4.8 Section 77A (11) of the Companies Act, 1956 states that *"If a company makes default in complying with the provision of section 77A or any rules made there under, or any regulations made under clause (f) of sub-section (2) of Sec 77A, the company or any officer of the company who is in default shall be punishable with imprisonment for a term which may extend to two years, or with fine which may extend to fifty thousand rupees, or with both"*. I note that prosecution u/s

77A(11) of the Companies Act, 1956 read with Sec 621(1) of the Companies Act, 1956 has also been initiated by SEBI against the company, Shri K. R. Naik, Chairman and Managing Director, Shri Dattaraj V Salgaocar, Director and Shri K. G. Prabhu, Company Secretary, the officers responsible for the above default.

4.9 From the facts and circumstances stated above, I find that there was no intention to buy-back by the company despite passing the resolution in the specially convened EGM and having enough opportunities to do the same. Further by not intimating the failure to buy- back not even through the Annual Report, which is required as per the provisions of section 217(2B) of the Companies Act, 1956, fortifies the finding that there was never an intention to buy-back the shares and the announcement thereof was only for the purpose of misleading the investors. This act of the company amounted to sending out false or misleading information by the company when it did not intend to implement the resolution. In view of the above, aforesaid acts of DIL construe as misleading information to the public which is in violation of Regulation 5(1)(a) of FUTP Regulations, 1995 which states that no person shall make any statement or disseminate any information which is misleading in a material particular which induces sale or purchase of securities.

4.10 Apart from the above, DIL has raised a contention that since the alleged violations had taken place on or about October 4, 2002, no action can be taken against DIL under section 11 (4) (b) of the SEBI Act as its retrospective application to the present case will not be applicable. I have noticed from the investigation and the submissions made by DLink that there has been violation of the provisions of SEBI (Prohibition of Fraudulent and Unfair

Trade Practices relating to Securities Market) Regulations, 1995. These violations would warrant action against the noticees under the provisions of Section 11 (4) (b) of SEBI Act, 1992. I have noticed that one of the submissions made by the noticees is that the provisions of Section 11 (4) (b) were brought into the SEBI Act, 1992 with effect from October 29, 2002 whereas, the alleged violations had occurred during October 04, 2002, rendering the said provision inapplicable to the said violations, if any. I am of the view that the orders passed under Section 11 (4) (b) cannot only be restricted to emergent circumstances but can also be invoked in situations which warrant action post facto. Any action which SEBI would be required to take now though post facto would still ensure appropriate remedy of the violations committed by the noticees. Also, the provisions of Section 11 (4) (b) inserted into the SEBI Act, 1992 with effect from October 29, 2002 is only an explanation or elucidation of the powers already vested in SEBI under Section 11 of SEBI Act, 1992. Consequently, the power to take action under Section 11 (4) (b) is only an existing power already vested with SEBI under Section 11 of the SEBI Act, 1992. Therefore, the action taken pursuant to the show cause notice issued under Section 11 (4) (b) would be valid. This view of SEBI has been confirmed by the High Court of Calcutta in WP No. 1933 of 2004 - *Raj Kumar Kishorepuria Vs SEBI (AIR 1997 Cal 308)* whereby it has held that:

The measures indicated in clauses (a) to (d) of Regulation 11 are, in substance, identical with the already existing ones mentioned in clause (a) to (d) of section 11(4) of the Act. In the clauses some powers of the Board were enumerated specifically, without prejudice to the general power given to it by section 11 and 11B of the Act. They are powers to suspend, restrain and impound; by their very nature, powers to be exercised as interim measures. They are not punishments or penalties proper, as the terms denote in the context of a legally punishable offence or misconduct.

4.11 In this regard, I also rely on the judgment of Hon'ble SAT in the matter of *Karvy Stock Broking Ltd.* wherein it was held that -

“Even under section 11(1) and thereafter with the introduction of section 11B in the year 1995, the power of the Board was very wide and it could take every measure that a situation would demand and issue such directions that it considered necessary including the suspension of an intermediary. Yet, to put everything beyond the shadow of doubt, even the implicit has been made explicit by adding sub section (4) in Section 11 which now expressly authorizes the Board to issue various kinds of orders, “either pending investigation or enquiry or on completion of such investigation or enquiry”.

... .. As already observed, section 11 is the very heart and soul of the Act. This provision has been periodically amended and today it is substantially different from what it was at its inception in the year 1992. The scope of the power has been considerably widened. The introduction of sub section (4) in section 11 and various other provisions like section 11B is indicative of the legislative intent. These provisions are meant to arm the Board with authority so as to be able to effectively exercise power and achieve the declared objectives of the Act.”

4.12 In view of the above observation made by Hon'ble SAT, I find that DIL's submission is not acceptable.

5.0 Order

5.1 In exercise of powers conferred upon me in terms of Section 19 of SEBI Act, 1992 read with Section 11, 11B of the SEBI Act, 1992 and Regulation 5 (1) (a) of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 1995, read with Regulation 11 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003, I hereby direct D-Link India Ltd. not to buy, sell or deal in securities, in any manner, directly or indirectly, for a period of one month.

4.2 This order shall come in force with immediate effect.

Place : Mumbai

T.C. Nair

Date : 21.08.2007

Whole Time Member

Securities and Exchange Board of India