

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA

CORAM: V. K. CHOPRA, WHOLE TIME MEMBER

**IN THE MATTER OF VITAL COMMUNICATIONS LTD., SHRI J. P. MADAAN,
SHRI R. K. GARG, SMT. SUBHA JHINDAL, SHRI VINAY TALWAR AND SHRI
VIJAY JHINDAL**

IN THE SCRIP OF VITAL COMMUNICATIONS LTD.

DATES OF HEARING: August 14, 2007, August 31, 2007 and October 12, 2007

APPEARANCES:

FOR THE NOTICEES:

1. Shri S. K. Jha, Practicing Company Secretary (for Vital Communications Ltd.)
2. Shri V. K. Kaushik, Practicing Chartered Accountant (for Shri Vijay Jhindal)
3. Shri Bir Shankar, Practicing Company Secretary (for Shri R K Garg and Smt Shubha Jhindal)
4. Shri J P Madaan

FOR SEBI:

1. Smt Barnali Mukherjee, DGM
2. Shri Naveen Sharma, Manager
3. Shri Mohamed Rahaz P. M., Legal Officer

ORDER

Under Section 11B of the SEBI Act, 1992 and Regulation 11 of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to the Securities Market) Regulations, 1995

1. Securities and Exchange Board of India (hereinafter referred to as "SEBI") conducted investigation into the misleading advertisements issued by certain companies including Vital Communications Ltd. (hereinafter referred to as "VCL.")

2. VCL is a Delhi based company established in the year 1995 by Shri Vinay Talwar. It came out with an Initial Public Offering of 20 lakh equity shares of Rs. 10 each in December 1995 and was subsequently listed on the Delhi Stock Exchange on February 26, 1996. VCL was listed on the Bombay Stock Exchange Ltd. (hereinafter referred to as "BSE") in May 2000 and the National Stock Exchange of India Ltd. (hereinafter referred to as "NSE") on March 7, 2001. The shares were also listed on the Jaipur and Ahmedabad Stock Exchanges.
3. Investigations revealed that VCL had issued advertisements in various news dailies during May and June 2002 indicating that a meeting of its Board of Directors was to be held shortly to *inter-alia*, consider buyback of its shares, issue of bonus shares and preferential issue of shares. Following is the list of advertisements and their dates of publication:

Date of Issuance of advertisement	Date appeared in newspapers	Newspaper	Matter in the Advertisement
20/5/02	May 27 and 28, 2002	Economic Times	Buyback up to 10,00,000 shares at max price of Rs. 30
	May 29, 2002	Business Standard	
27/5/02	May 28, 2002	Business Standard	Preferential allotment of equity shares up to 20,00,000 at the rate of Rs. 35 (Market price at BSE Rs. 7.55)
	May 29, 2002	Economic Times	
17/6/02	June 24, 2002	Economic Times	Issue of Bonus share in the ratio of 8:10

4. Subsequent to the publication of the advertisements, VCL informed the respective Stock Exchanges that while the proposals of buyback of shares and issue of bonus shares were rejected by its Board of Directors, preferential allotment of shares had been approved. However, the preferential allotment was

made at just Rs. 10 per share as against the advertised rate of Rs. 35 per share.

5. The advertisements issued by VCL were questionable on two counts:
 - a) The advertisements were issued at the proposal stage itself, which is not a statutory requirement.
 - b) All the proposed corporate actions were contradictory to each in nature i.e. buyback reduces the number of outstanding shares while preferential allotment and bonus issue increases the number of outstanding shares.
6. Show Cause Notices dated May 24, 2005 were issued to VCL, Shri J P Madaan, Shri R. K. Garg, Smt. Subha Jhindal, Shri Vinay Talwar and Shri Vijay Jhindal (hereinafter collectively referred to as “the Noticees” and singularly by their individual name) asking them to show cause as to why appropriate direction under Sections 11 and 11B of the SEBI Act, 1992 including a direction debarring them from accessing the capital market and trading in securities should not be issued against them for alleged violations Regulations 4, 5(1) & 6 of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Markets) Regulations, 1995 (hereinafter referred to as the “PFUTP Regulations”).
7. No replies to the Show Cause Notices were received from any of the Noticees within the stipulated time period of 21 days and therefore a reminder dated June 7, 2007 was sent to the entities. Consequently, in absence of receipt of reply from the Noticees, the Show Cause Notice was posted on the SEBI website on June 25, 2007 giving 21 days time to the Noticees to reply to the same. Again, no reply was received from the Noticees.
8. Opportunities of personal hearing were provided to the Noticees on August 14, 2007, August 31, 2007 and October 12, 2007 respectively. On October 12, 2007, Shri S K Jha, practicing Company Secretary (on behalf of VCL), Shri V. K.

Kaushik, practicing Chartered Accountant (on behalf of Shri Vijay Jhindal), Shri Bir Shankar, practicing Company Secretary (on behalf of Shri R K Garg and Smt Shubha Jhindal) attended the personal hearing. Shri J P Madaan appeared personally and filed written submission as well. Adjournment was sought by the other Noticees but request for the same was denied and 15 days time was given to all of them to file written submissions. However, no submissions have been received till date from any of the Noticees except from Shri Vijay Jhindal.

9. In his written submissions filed on October 12, 2007 Shri J. P. Madaan *inter alia*, submitted that:

- He was never a shareholder of the company, never dealt in VCL scrip and is currently not associated with the company.
- He was inducted as an employee of VCL and later appointed as a director but he was not aware of the financial operations of the company.
- The preferential allotment of shares (on December 14, 1999) was made before he became the director and the impugned advertisements made by VCL were made without the knowledge of the Board of Directors. He further asserted that he had no knowledge that the shares had been sold in the open market.
- He had resigned as whole time director from March 31, 2007 and continued as an independent director until June 30, 2007.
- An external Chartered Accountant had advised VCL that due to non fulfilment of provisions of the Companies Act, 1956 and SEBI Act, 1992, buyback of shares was not possible.

10. Vide letter dated December 5, 2007 Shri Vijay Jhiindal submitted that his relationship with VCL existed only up to May 17, 2001 and that he was not involved in the issuance of the impugned advertisements. He also furnished Form 32 to show that he resigned from the company w.e.f. May 17, 2001. Shri Vijay Jhindal, vide letter dated February 12, 2008 reiterated his earlier

submissions.

11. Smt. Shubha Jhindal vide letter dated February 12, 2008 submitted that she was appointed as an additional Director of VCL on July 5, 2002 and therefore she is not responsible for any acts of the company prior to the date of her appointment.
12. I have carefully examined the investigation report, Show Cause Notices and the additional written submissions made by the Noticees and find that VCL had issued three separate advertisements in various newspapers regarding the proposed buy back, preferential allotment and bonus issue of shares.
13. The first advertisement dated May 20, 2002, published on May 27, 2002 stated that the meeting of the Board of Directors of VCL was going to be held on June 4, 2002 at Mumbai to consider buyback up to 10 lakhs shares at a maximum price of Rs. 30 per share from the reserves of over Rs. 7 crores available with VCL. The graphics in the advertisement indicated as if Foreign Institutional Investors (FII's) have increased their holding in the company. However, on investigation of the shareholding pattern of the company it was found that FII's never had a stake in the company at any point of time.
14. It was also mentioned in the advertisement that the proposed buyback of shares was approved by an expert committee. From the material available on record, I however find that the committee had submitted a one page report to VCL merely stating the basic rules and regulations regarding buyback of shares. The report stated that there should be provision for buyback of shares in the Articles of Association (AoA) (as per section 77A (2) of the Companies Act, 1956). But there was no such provision in AoA of the company. Despite this fact, VCL went ahead and published the advertisement at the proposal

stage itself.

15. The second advertisement dated May 27, 2002 and published on May 28 and 29, 2002 pertained to the Board meeting to be held on June 14, 2002 at Bangalore to consider the preferential allotment of up to 20 lakhs shares to the promoters at the rate of Rs 35 per share. The graphics in the advertisement indicated an increase in turnover, Earnings per Share (EPS), profit and FII shareholding. However, an examination of the Profit & Loss Account of the company for the financial year 2001-2002 revealed that the income, Profit after tax and EPS of VCL had decreased in the financial year 2001-2002 as compared to the previous financial year, contrary to the indications given in the advertisement.
16. The preferential allotment of shares was approved in the board meeting on June 14, 2002 when VCL was still considering buyback of shares. The preferential allotment was however approved at a price of Rs. 10 against the stated price of Rs. 35 in the advertisement, again indicating that the advertisement was an attempt to benchmark the price of the scrip to the levels of Rs. 30- Rs. 35 when the scrip was actually trading in the range of Rs.5- Rs. 10. It is evident from examination of the advertisements that VCL was intentionally issuing misleading advertisements to induce demand for its shares in the market.
17. The third advertisement dated June 17, 2002 and published on June 24, 2002 informed the public that a board meeting would be held on July 5, 2002 at Hyderabad to consider the issue of bonus shares in the ratio of 8:10. At the time of issue of this particular advertisement, VCL was not eligible for issuing bonus shares as it's paid up capital consisted of partly paid up shares. When questioned on the ratio of the bonus issue, VCL explained that since it was

expecting its total reserves to be approximately around Rs. 8 crore, it was decided that the ratio for issue of bonus shares would be 8:10. It is pertinent to note that in their advertisement regarding buyback of shares VCL had mentioned using available reserves of Rs. 7 crore for the purpose of buyback and at the time of issue of bonus shares, they indicated that the reserves were approximately around Rs. 8 crore. However the balance sheet of VCL for financial year ending March 31, 2002 clearly shows that as against all the claims made in their advertisements, the actual reserves available with VCL were just about Rs. 4.68 crores.

18. Perusal of the previous annual reports particularly of financial year 2001- 2002 of VCL indicated more than 100 times increase in the advertisement expenditure for the financial year 2002-2003. Such extremely unusual and drastic increase in the budget for advertisement expenses as compared to previous financial years, especially for an unwarranted and non stipulated expenditure on a particular corporate action itself clearly indicates the manipulative intent of VCL and its directors.
19. I note that, all these advertisements were made at the proposal stage itself which is not statutorily warranted. VCL had not issued any such advertisements in the past and expenses incurred on these advertisements were unusual. The claims made in these advertisements did not match the actual financial position of VCL as indicated from an examination of its financial reports. Moreover, all the proposals, as indicated in the advertisements were later rejected by the VCL Board and no clear explanations were provided for these rejections.
20. The common thread between all the above mentioned corporate actions and the manner of their advertisement is that a favourable financial picture of VCL was

being presented before the investors to positively influence the prices and volumes of the scrip. The advertisement signalled to the market that the fair value of VCL shares was much more than market price which propelled the investors to transact more in VCL scrip. Due to these announcements, the price and volume in the scrip registered a sharp increase and subsequently, entities related to the company offloaded their shares during this period. This chain of events clearly indicates the malafide intention on part of VCL and its directors to defraud its investors.

21. I have examined the price and volume data of the VCL scrip at BSE and find unusual movements in the price and volume of the scrip between April 1, 2002 and August 31, 2002, the time period in which the advertisements pertaining to buyback, preferential allotment and bonus shares were issued by VCL. On the basis of price volume data of the scrip, the investigation period was divided into four time periods as under:

Time Periods	Period	Average Share Price	Average Volume	Average No. of Trades
Time Slot 1	April 1, 2002 to April 26, 2002	3.46	16, 795	57
Time Slot 2	April 29, 2002 to May 20, 2002	11.12	3, 44, 216	910
Time Slot 3	May 21, 2002 to July 15, 2002	8.10	10, 29, 090	1, 965
Time Slot 4	July 16, 2002 to August 31, 2002	3.53	40, 440	131

22. It was observed that in the second time period (the 20 day period prior to publication of advertisements) price and volume in the scrip suddenly shot up as compared to the price and volume prevailing in the first period. The major selling clients during this period were S V Stock Land, Anupama Communications Pvt. Ltd., Fashion Tech India Ltd., Troop Trac Marketing Ltd.,

Rajat Stock Investment Pvt. Ltd. All these clients except S V Stock Land were allotted preferential shares of VCL in 1999 and were also related entities of VCL.

23. The preferential allotment in 1999 took place on December 12, 1999 when VCL allotted 72 lacs equity shares of Rs. 10 each on a premium of Rs. 2.5 as detailed below:

S. No.	Name	No. of shares allotted	Amount received (Rs.)
1	Anupama Communications Pvt. Ltd	2, 00, 000	25, 00,000
2	Brut Finance(India) Pvt. Ltd.	5, 00,000	62, 50,000
3	Chankya Apparels Pvt. Ltd.	5, 00,000	62, 50,000
4	Chankya Overseas Pvt. Ltd.	5, 00,000	62, 50,000
5	Cosmo Corporate Services Ltd	5, 00,000	62, 50,000
6	Fashion Tech India Ltd.	5, 00,000	62, 50,000
7	Flair Finance(India) Ltd.	5, 00,000	62, 50,000
8	Heritage Corporate services Ltd.	5, 00,000	62, 50,000
9	Perfect Car Scanners Pvt. Ltd.	5, 00,000	62, 50,000
10	Rajat Stock Investment Pvt. Ltd.	5, 00,000	62, 50,000
11	Troop Trac Chits Pvt. Ltd.	5, 00,000	62, 50,000
12	Troop Trac Exports Pvt. Ltd.	5, 00,000	62, 50,000
13	Troop Trac Electrodes Pvt. Ltd.	5, 00,000	62, 50,000
14	Troop Trac Marketing Pvt. Ltd.	5, 00,000	62, 50,000
15	Wisdom Publishing Pvt. Ltd.	5, 00,000	62, 50,000
	Total	72, 00,000	9, 00,00,000

24. The above 15 companies were shown as supplier to VCL though their business objectives and interests are varied, ranging from construction to publishing to financing which is different from the business of VCL i.e. software development. The Department of Company Affairs (now known as “Ministry of Corporate Affairs”) while inspecting the accounts of VCL found that company had used its funds indirectly for the purchase of its own shares. The company gave advances to Anupama Communications Pvt. Ltd and CBS

Systems Pvt. Ltd for development work and both these companies in turn gave trade advances to the above mentioned 15 companies (on the pretext of getting their work done). The same money then came back to VCL as share application money, thereby clearly violating Section 77 of the Companies Act, 1956.

25. At the time of opening their demat accounts, all the above mentioned 15 entities had given one common address on their application form clearly indicating the relationship between the entities. It was also found that Shri Vinay Talwar was the introducer to some of these companies at the time of opening of their bank accounts. From the documents submitted in connection with the preferential allotment by VCL, it was observed that Shri Vinay Talwar was also the chairman of VCL at the time of the preferential allotment in December 1999. Further, Shri Ram Singh served as director for both S V Stockland and Rajat Stock Investment. It becomes increasingly irrefutable, in light of all this evidence, that there exists a link between VCL, its promoters and these 15 entities. By trading among themselves in the scrip of VCL, these entities created artificial volumes in the market.
26. From the above sequence of events and materials available on record, it is clear that the Noticees had a pre determined plan to raise the price and volume of the VCL scrip. This fact is further established from the statement dated March 11, 2004 of Shri Vinay Talwar, former Chairman of VCL who in his statement has alleged that Shri Vijay Jhindal was behind all the malafide activities of VCL. Shri Vinay Talwar stated that Shri Vijay Jhindal was brought in as a co-promoter of VCL in April 1998. As per the MOU signed with Shri Vijay Jhindal, he was supposed to bring in Rs 90 lakhs and take care of all the financial and legal matters of VCL. He was also to bring in a third party to invest funds in VCL. But he could not bring the promised funds to

VCL and therefore suggested that a preferential issue of VCL shares should be made which would be subscribed to by some entities known to him or his associates and their companies. It was Shri Vijay Jhindal who had transferred funds from the company to the entities known to him through CBS Systems Pvt. Ltd. and Anupama Communications Pvt. Ltd. The details of the fund flow through these entities are explained above at paragraph 24.

27. Subsequent to this fraudulent preferential allotment made in 1999, VCL, to raise further funds issued misleading advertisements to attract the investors. As a result of the impugned advertisements, innocent investors started trading in the VCL scrip. By using the situation to their advantage, the related entities offloaded the shares purchased by them utilising the funds provided by the company. Time Slot 3 clearly indicates this. During this period, the average volumes traded in the scrip doubled while the prices decreased marginally when compared to Time Slot 2. During this time period, related entities offloaded around 68 lakh shares in the market.
28. Shri Vijay Jhindal submitted that he was not a director of VCL at the time when the advertisements were issued. He also produced Form 32 to show that he had resigned from the company w.e.f. May 17, 2001. He also produced a receipt dated June 6, 2001 to show that the company had filed the Form 32 with Registrar of Companies, Delhi. On examination of the records available with the ROC, I find that the company had filed Form 32 only on June 6, 2002 and not on June 6, 2001 as submitted by Shri Vijay Jhindal. It is thus very clear that Shri Vijay Jhindal tried to mislead SEBI by submitting forged receipt of the RoC suggesting that Form 32 was filed by him on June 6, 2001 as against the fact that the same was filed on July 6, 2002.
29. Smt. Shubha Jhindal vide letter dated February 12, 2008 contended that she

was not responsible for the acts of the company prior to her appointment as the additional Director on July 5, 2002. on examination, I find that the Board meeting for considering the bonus issue was held on July 5, 2002. At this point of time, Smt. Shubha Jhindal was already the additional director of VCL and therefore she cannot claim absolution from the entire charge levelled against her.

30. I however do not find any cogent evidence pointing to the involvement of Shri Vinay Talwar in the entire matter. In his statement dated March 11, 2004, Shri Vinay Talwar stated that Shri Vijay Jhindal had orchestrated his removal from the directorship of the company when Shri Talwar had come to know of the wrongful transactions undertaken by Shri Vijay Jhindal and thus asked him to return the money borrowed by him from the company. I have also observed that as regards his role in the preferential allotment in the year 1999, a separate investigation has been initiated and the findings recorded in the present order against him are prima facie in nature and without prejudice to the proceedings already pending against him.
31. I find from the Annual Report of the company for the financial year 2002-2003 that Shri Vijay Jhindal and Shri Vinay Talwar were not the directors of the company at the time when the malafide and fraudulent transactions took place. Though Shri Vijay Jhindal had resigned from the company, I find evidences linking Shri Vijay Jhindal in the manipulative transactions of the VCL shares just prior to and after the period when the impugned advertisements were issued. From the bank accounts of the seller entities mentioned above at paragraph 22, it was found that part of the money received from the brokers for the selling was transferred into the account of Master Finlease Ltd. an entity owned by Vijay Jhindal, his wife and his mother, as shown below:

Inflow in the a/c of Master Finlease				The entities from whom received	
Amount	Instrument No.	Date	From*	Date	From
20, 00,000	133185	1 st July 2002	Flare Finance	1 st July	S V Stock Land
40, 00,000	120716	5 th July, 2002	Troop Trac Marketing Ltd.	5 th July	Anupama Communications
				5 th July	Perfect Car Scanners
10, 00,000	120670	15 th July, 2002	Perfect car scanners	13 th Jul	S V Stockland
35, 00,000	120717	18 th July, 2002	Troop Trac Marketing Ltd.	17 th Jul	SV Stock Land
				15 th Jul	Fashion Tech

32. The related entities sold total 71.14 lakh shares into the market between May 2, 2002 and July 31, 2002, as stated below, taking advantage of the artificial interest created by the impugned advertisements:

Broker	Sub Broker	Client	Net Sales
VSE Securities Ltd.	Thakkar Stock Brokers Pvt. Ltd.	S V Stock land	27, 26,591
UPSE Ltd.	Saroj & Co.	Fashion Tech India Ltd.	10, 78,025
		Perfect Car Scanners	2, 00,000
		Anupama Communications Ltd.	74,725
TCP	NA	Rajat Stock Investment Pvt. Ltd	11, 00,022
Integrated Master Securities Ltd.	NA	Troop Trac Exports Pvt. Ltd.	18, 71,345
Total			71, 41,208

33. The funds flow to Master Finlease, an entity owned by Shri Vijay Jhindal from related entities indicates that the Shri Vijay Jhindal was involved in the matter and committed fraud on innocent investors by allowing his own entity to be used as a conduit and thus actively participated in creation of artificial market

in the scrip and thereby violated Regulations 4 and 6(a) of PFUTP Regulation.

34. After reading the facts as presented before me, I feel that the sequence of events can be best summarised as below. In the year 1999, VCL financed the subscription of its own preferential issue through related and associated entities. Subsequently, after the company issued various misleading advertisements between May and June 2002, the entities who had been allotted shares during the preferential allotment in December 1999, taking advantage of the inflated prices at which the VCL scrip was trading in the market, offloaded their shares, creating artificial semblance of trading activity in the scrip.
35. The entire chain of events with respect to the buyback, bonus issue and preferential allotment of shares, the unwarranted advertisements, extent of monies spent, reasons for the proposed corporate actions, reasons for the proposal being rejected, impact on the price and volume of the shares is highly suggestive of an orchestrated ploy on part of the directors viz. Shri J P Madaan, Shri R K Garg, Smt Subha Jhindal to create an artificial demand for VCL shares and induce innocent investors to purchase VCL shares sold by the promoters and their related entities.
36. The response of the company and its representatives has been evasive and the denial of responsibility as director by officials of the company like Shri J.P. Madaan is uncalled for. I thus find that Shri J P Madaan, Shri R K Garg, Smt Subha Jhindal, have violated provisions of Regulation 3, 4, 5(1) & 6(a) of PFUTP Regulations whereas Shri Vijay Jhindal has violated 6(a) of PFUTP Regulation.
37. Taking into consideration the facts and circumstances of the case, in exercise of the powers conferred upon me under Sections 11B and 19 of the SEBI Act 1992 read with Regulation 11 of the SEBI (Prohibition of Fraudulent and Unfair

Trade Practices Relating to Securities Market) Regulations, 1995, I hereby drop the charges against Shri Vinay Talwar (PAN No. AAAPT0316L) in these proceedings. As regards Smt. Shubha Jhindal, her involvement was confined to the issuance of bonus shares only and therefore I am inclined to impose a lesser penalty on her. Accordingly, I hereby restrain Smt Shubha Jhindal (PAN No. AAGPJ0051N) from accessing the securities market and prohibit her from buying, selling and dealing in securities in any manner for a period of six months.

38. As regards the remaining Noticees i.e. Vital Communications Ltd. and its Directors Shri J P Madaan (PAN no. AIAPM8977E), Shri R K Garg, and Shri Vijay Jhindal (PAN No. AADPJ9438J), I hereby restrain them from accessing the securities market and prohibit them from buying, selling and dealing in securities in any manner for a period of two years.
39. This order shall come into force with immediate effect.

Date 20th February, 2008

Place: Mumbai

V. K. CHOPRA
WHOLE TIME MEMBER
SECURITIES AND EXCHANGE BOARD OF
INDIA