WTM/PS/ 08 /IVD1/OCT/2009

BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA, MUMBAI

CORAM: MR. PRASHANT SARAN, WHOLE TIME MEMBER

AGAINST PREMIUM CAPITAL MARKET AND INVESTMENTS LIMITED IN THE MATTER OF CONSORTEX KARL DOELITZSCH (I) LTD.

Date of hearing: July 7, 2009

Appearance:

Noticee: Mr. S. K. Bandi, Director

For SEBI: Mr. Shashikant, Legal Officer (Presenting Officer)
Mrs. Medha Sonparote, Deputy General Manager
Mr. Sachin Yadav, Assistant General Manager
Mrs. Kshama Wagherkar, Legal Officer

ORDER

UNDER SECTION 11, 11B OF THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 READ WITH REGULATION 13 OF THE SEBI (MERCHANT BANKERS), REGULATIONS, 1992

1. Securities and Exchange Board of India (SEBI) conducted investigations into the alleged irregularities in the public issue of Consortex Karl Doelitzsch (I) Ltd. (hereinafter referred to as "Consortex"), formerly known as Andhra Pradesh Power Tools Ltd. Consortex came out with a public issue of 1,68,80,500 equity shares of Rs.10 each for cash at par aggregating to Rs.1688.05 lakh. The issue opened for subscription on January 22, 1996 and closed on January 27, 1996. The prospectus of Consortex stated that 36,00,000 equity shares of Rs.10 each for cash at a premium of Rs.5 per share were reserved for allotment to the foreign collaborators i.e. Consortex Karl Doelitzsch, Germany (Consortex, Germany) with a lock in period of 5 years.

2. Premium Capital Market and Investments Ltd. (hereinafter referred to as "Premium") was appointed as a Co- Lead Manager to the issue along with the Lead

Manager, M/s. Keynote Corporate Services Ltd. (Keynote). Premium was responsible for the post issue activities at the time of public issue of Consortex. The investigations revealed that the amount to be invested in the company by the foreign collaborator before the public issue opened was never invested in accordance with Section L of the SEBI (Disclosure and Investor Protection) Guidelines, 1992. The same was invested by a domestic company, Volkskas Mercantile Ltd. (VML). An auditor's certificate dated January 19, 1996 stated that the promoters had brought in their contribution. However, no independent verification was done by Premium.

3. Investigations further revealed that Consortex availed a loan of Rs. 50 lakh from Fairgrowth Financial Services Ltd. (Fairgrowth). Fairgrowth had filed a suit for its dues amounting to approx. Rs.84 lakh including interest. Premium did not inform SEBI that the public issue proceeds were attached by a Court order dated January 23, 1996 on the basis of a suit filed which was subsequently vacated in March 1996. Premium did not disseminate the information to the public through advertisement in the newspapers and /or individual letters. It was alleged that Premium had failed in their post issue obligations and thus violated provisions of Regulations 13 read with Clause 2 of Schedule III of SEBI (Merchant Bankers) Regulations, 1992. It was also alleged that Premium had violated SEBI Circular dated March 1, 1993, which briefly, states that a lead manager responsible for post issue activities shall *inter alia* maintain close co-ordination with RTI, monitor the flow of applications after closure of the issue, process the applications and other matters till the date of allotment is finalized, dispatched completed and listing is done, etc. Further any act of omission or commission on the part of any such intermediaries noticed during such visits should be duly reported to SEBI.

4. A show cause notice under section 11B of the SEBI Act, 1992 read with the Regulation 13 and clause 2 of the Code of Conduct of SEBI (Merchant Bankers) Regulations, 1992 dated January 30, 2004 was issued to Premium asking it to show

cause as to why a suitable direction debarring them from acting as an intermediary in the securities market for a particular period should not be passed.

5. Premium vide letter dated February 18, 2004 submitted as under:

    i. They were Co-Lead Manager to the issue along with other Lead Manager, M/s. Keynote Corporate Services Ltd. and were responsible for post-issue activities of the issue, viz., marketing of the issue, coordinating with Keynote Corporate Services Ltd., follow up with the various agencies like Registrar to the Issue, Banks, Intermediaries and listing of the instruments and dispatch of the certificate to the allottees.
    ii. With regard to the design of prospectus, letter of offer, advertising, publicity material including newspaper advertising containing features of letter of offer, completion of formalities with Stock Exchanges, Registrar of Companies including filing of documents with SEBI were the responsibilities of Keynote Corporate Services Ltd. The pre-issue responsibility of filling of the prospectus to the Registrar of Companies was handled by Keynote.
    iii. The issue opened on January 22, 1996. An auditor's certificate dated January 19, 1996 i.e. before the opening of the issue stated that the promoter had brought in their contribution on the same date. It specifically mentioned that the reservation made for firm allotment as per prospectus has been brought in. Since the auditor is an autonomous body regulated under the regulation of Institute of Chartered Accountants of India, they had relied upon their certificate.
    iv. As per DIP guidelines, any shortfall in firm allotment should be brought in by promoters before the issue opens and therefore Volkskas Mercantile one of the company of promoter's has subscribed the shares at premium in place of Consortex. This fact was not disclosed by the auditor in the certificate dated January 19, 1996 and they relied upon the same.
    v. For non-disclosure regarding Court case filed by Fairgrowth for their dues for Rs. 84.00 lakh approx. against the issuer company, has already been disclosed in the prospectus. Regarding attachment of Bank account of public subscription

was never been informed to them by any Bank nor by the issuer company and same has been vacated in the month of March and Bank has released the fund to the company account. It could not be reported as the said court order was never served upon them nor any bank has forwarded any intimation to them in this regard.

6. An opportunity of personal hearing was granted to the noticee before the then Whole Time Member on July 15, 2004. Vide letter dated July 13, 2004, the noticee made additional written submissions as under:

i. As regards firm allotment of 36 lakh shares reserved for foreign promoters /collaborators, there was a specific disclosure on page 13 of the prospectus that the unsubscribed portion would be taken by the promoter before issue opens and the same will be subject to lock-in period of 3 years and the money was brought in before the issue opens was supported by a certificate of a Chartered Accountant, and therefore nothing was doubtful.

ii. Their company has closed Merchant Banking Division since 1997 and their senior staff who were associated with the management of the issue have left the organisation. At present they are reviving their company by amending object clause to take BPO and outsourcing business. Their liquidity has already been exhausted due to the heavy losses resulting because of non-recovery of leasing finances and other outstanding book-debts.

iii. They have performed their duty diligently and therefore have requested SEBI to take a lenient view of the matter.

7. Due to change in the competent authority, the case was put afresh before me. Accordingly, another opportunity of hearing was granted before me to the noticee on July 7, 2009 wherein Mr. S.K. Bandi, Director appeared and reiterated the submissions made vide the above letters.

8. I have carefully considered the investigation report, the show cause notice, the reply and written submissions of the noticee. The issue to be determined is whether

Premium had failed in exercising due diligence while discharging its duties as a Co-Lead Manager to the issue.

9. I note that as per the capital structure of Consortex as disclosed in the prospectus, 36,00,000 equity shares of Rs.10 each for cash at a premium of Rs.5 per share were reserved for allotment to the foreign collaborator, Consrotex Karl Deolitzsech, GmbH, Germany and were required to be locked in for a period of 5 years. It was found that the money to be invested in the company by the foreign collaborator before the public issue opened was never invested in accordance with Section L of SEBI (Disclosure and Investor Protection) Guidelines, 1992 (DIP Guidelines).

10. Section L of DIP Guidelines states that *"the promoters' contribution shall not be diluted for a period of 5 years from the date of commencement of the production or date of allotment whichever is later. Promoters must bring in their full subscription to issue in advance before public issue."* I find that the money to be invested by the foreign collaborator before the public issue was never invested in Consortex by them before the public issue opened and the same was invested by a domestic company i.e. Volkskas Mercantile Ltd. (VML) on their behalf. Further, the auditor's certificate dated January 19, 1996 certified that reservation made on firm basis to NRI/OCBs/FIIs with repatriation benefits out of the subscription offered through the terms of prospectus have been brought in.

11. I note that the allegation against Premium is that as a co – lead manager to the issue, they failed to find out whether the foreign collaborator had actually brought in the investment as stated in the Prospectus before allotment of shares. Premium argued that as per the division of duties between the lead manager and the co-lead manager, the pre-issue responsibilities lay with lead manager handling pre issue activities, viz., M/s. Keynote Corporate Services Ltd. and that they relied upon the Chartered Accountants' (CA) certificate submitted by the said Lead Manager.

The argument that Premium relied on a certificate issued by a CA is flawed for the reason the CA certificate just stated in a generic way that Promoters, Directors, friends, relatives and their associates have brought in their capital contribution. It does not at all say anything about foreign collaboration in general or Consortex, Germany in particular. A pivotal investment cannot be decided on the basis of such a generalization. Premium at the very minimum should have enquired whether Consortex, Germany had made their promised contribution. I am of the opinion that the same required independent verification on the part of a Co- Lead Manager. Premium at least at the time of allotment of shares ought to have verified whether contribution from foreign collaborator had been received or not. I further note that if Premium would have come to know of this if they had cared to verify the list of 50 allottees. Therefore, I do not agree with the contention of Premium. At the very least, Premium bears its part of joint responsibility as enunciated in Annexure A - "interse allocation of duties" even if the demarcated area of work lay with the Keynote.

12. As regards the violation of SEBI Circular dated March 1, 1993, I find that even though Premium was responsible for marketing the issue and post issue activities, it should have nevertheless maintained a close coordination with the company and Registrar and Transfer Agents and verified at the time of allotment of shares whether the foreign collaboration from the foreign collaborator has been received or not. I find that Premium has violated the above circular by not disseminating the information to the investors and by not reporting the above omission on the part of the Lead manager to SEBI.

13. As regards the non disclosure of a suit filed against Consortex, I find that it was the responsibility of both the lead managers handling the issue to disclose the fact to the investors. I note that Premium came to know about this fact only when SEBI pointed this to them. Premium's contention that the fact of attachment of bank account was not brought to their notice by the bank or the company militates against the very concept of the due diligence. The investors and SEBI depend upon the due diligence carried out by

the lead manager/s in finding out everything concerning the issue that is material to the issue.

14. To summarize, there are two allegations against Premium, firstly, it failed to bring to SEBI's notice that no investment was made by the proposed foreign collaborator, Consortex Karl Doelitzech, GmbH, Germany. Secondly, it failed to bring to SEBI's notice the fact of attachment of public issue proceeds vide court order in the matter of suit filed by Fairgrowth Financial Services for recovery of a loan given to the issuer company. Premium's defence in the case of the first allegation is that it was responsible for the post issue activity and entirely relied on the chartered accountant's certificate. For the second allegation, Premium's defence is that the concerned bank or the company did not bring the fact of attachment to their notice. I note that the proviso to Regulation 20 (1) of SEBI (Merchant Bankers) Regulation, 1992 states -

"*Provided that, where there are more than one lead merchant bankers to the issue the responsibilities of each of such lead merchant bankers shall clearly be demarcated and a statement specifying such responsibilities shall be furnished to the Board at least one month before the opening of the issue for subscription.*"

15. The question is whether "the requirement that responsibilities of each of the lead managers should be clearly defined" should be interpreted to mean that they are individually responsible for their own area of work and there are no joint responsibilities of co-lead managers. Such an interpretation will not be proper for the following reasons:

i The format of due diligence certificate to be given by lead managers is given in Annexure A of SEBI's circular dated December 24, 1992. After the perusal of the format, it is observed that it is a joint declaration by all the lead managers appointed to the public issue.

ii The term "lead manager(s) to the issue" gives the impression of joint and several responsibilities on the lead manager(s) to the issue. An investor e.g. might see four co-lead managers in an offer document. One of them might be a well known and respected name while the other three are

unknown. The impression he would carry is that issue is managed by responsible lead managers. If the responsibilities are not joint and several, the investor might face the prospect of the 'respected name' disowning all responsibility except what was formally allocated to him.

16. Reference is drawn to the interpretation made by Supreme Court in the matter of Chander Kanta Bansal vs. Rajinder Singh Anand (2008) 5 SCC 117 as under:

> *"16. The words "due diligence" have not been defined in the Code of Civil Procedure, 1908. According to Oxford Dictionary (Edn.2006), the word "diligence" means careful and persistent application or effort. "Diligent" means careful and steady in application to one's work and duties, showing care and effort. As per Black's Law Dictionary (18th Edn), "Due diligence" means the diligence reasonably expected from, and ordinarily exercised by, a person who seeks to satisfy a legal requirement or to discharge an obligation. According to Words and Phrases by Drain-Dyspnea (Permanent Edn. 13-A) "due diligence", in law, means doing everything reasonable, not everything possible. "Due diligence" means reasonable diligence; it means such diligence as a prudent man would exercise in the conduct of his own affairs."*

17. From the above, I find that Premium has not adhered to high standards of services, exercise of due diligence and proper care while dealing with the public issue and has violated Regulation 13 read with clause 2 of Schedule III of the Code of Conduct specified in the SEBI (Merchant Bankers) Regulations, 1992. I am of the view that due diligence on the part of lead manager and co–lead managers does not mean passively reporting whatever is reported to them but to find out everything that is worth finding out. As co lead mangers, they are jointly and severally responsible with the lead manager. I find that due diligence is about making an active effort to find out material developments that would affect the interests of investors. It is on the faith that intermediaries have conducted due diligence that public invests in the company.

18. I note that Premium Capital Market and Investments Ltd. was registered with SEBI as a Category I Merchant Banker with SEBI Registration No. INM000001907 and

has closed the Merchant Banking Business since 1997. I also note that the certificate of registration of Premium has expired on July 31, 1999 and it is not a registered intermediary with SEBI till date in any capacity.

19. Having regard to the nature and gravity of the charges established, the facts and circumstances of the case, I, therefore in exercise of the powers conferred upon me by virtue of Section 19 of the SEBI Act, 1992 read with section 11B and 11(4) of the SEBI Act, 1992, warn Premium Capital Market and Investments Ltd. to be careful and cautious in its dealings in the securities market in future and adhere to and comply with all relevant statutory provisions. I also direct Premium Capital Market and Investments Ltd. to note that any instances of violation or non-compliance of the SEBI Act and Rules and Regulations in future shall be dealt with stringently.

DATE: 12.10.2009
PLACE: MUMBAI

PRASHANT SARAN
WHOLE TIME MEMEBER
SECURITIES AND EXCHANGE BOARD OF INDIA