

**BEFORE THE SECURITIES AND EXCHANGE BOARD OF INDIA
CORAM: MADHABI PURI BUCH, WHOLE TIME MEMBER
FINAL ORDER**

**Under Sections 11, 11(4) and 11B of the Securities and Exchange Board of India
Act, 1992**

**In Re: Securities and Exchange Board of India (Prohibition of Fraudulent and
Unfair Trade Practices Relating to Securities Market) Regulations, 2003**

In respect of:

S.No.	Name of the Entity	PAN	CIN/DIN/ Firm Registration No.
1.	Celestial Biolabs Ltd.	AABCC4698Q	L72200TG1997PLC028374
2.	Dr. Aditya Narayan Singh	AITPS2152A	01756827
3.	Ms. Padma Singh	BIQPS8097A	01448915
4.	Lakshmi Purna & Associates	-	012323S

In the matter of Celestial Biolabs Ltd.

BACKGROUND

1. Celestial Biolabs Limited (hereinafter referred to as '**CBL / company / Noticee No. 1**') is a biopharmaceutical company primarily engaged in bio-pharma product development. The business plan of the company is essentially based on the production and supply of the biotechnological products. CBL formulates and manufactures ayurvedic proprietary products for the domestic market. CBL came

with an initial public offer in 2006 to raise funds amounting to approximate ₹ 30 crore. The company is listed on BSE and National Stock Exchange of India Ltd.

2. Dr. A. N. Singh is the Chairman and Managing Director of the company. He along with his family holds 37.31% as on March 31, 2017 which constitutes the Promoter Group of the company. The shareholding pattern of the company is as under:

Category of shareholder	Year ended March 31, 2012		Year ended March 31, 2011	
	No. of Shares	% to total share holding	No. of Shares	% to total share holding
Promoter Holding	55,57,178	38.06	55,72,178	44.93
Non-Promoter Holding	90,45,822	61.94	68,30,822	55.07
Total Share Holding	1,46,03,000	100.00	1,24,03,000	100.00

3. From the disclosures made by the company in its Annual Reports, the following is the composition of the Board. Other than Dr. A. N. Singh and his wife, Mrs. Padma Singh, all other Directors are shown to be Independent Non-Executive Directors.

Year	Managing Director	Other Directors			
2009-10	Dr. A N Singh	Mrs. Padma Singh	Dr. Jeetainder Roy Gour	Dr. D C Sastry	Dr. B Siva Kumar
2010-11				-	
2011-12				-	
2012-13				-	
2013-14				Dr. D C Sastry	-
2014-15				-	-
2015-16				-	-

From financial year 2010-11 onwards, the financial statements have been audited by M/s Lakshmi Purna & Associates, Chartered Accountants.

4. Securities and Exchange Board of India (hereinafter referred to as '**SEBI**') received a reference dated May 19, 2015 from the Office of Commissioner of Customs, Central Excise and Service Tax against CBL. Based on the investigation of the

Commissionerate, it was observed that the books of accounts of the company was being tailored to a considerable extent and various fictitious transactions were recorded by the company in the name of Bio-IT Services to project a rosy picture of the company to its shareholders.

5. Pursuant to the aforesaid reference, a detailed examination was carried out by SEBI to ascertain whether books of accounts of company were manipulated by way of fictitious transactions to project a rosy picture of the company to the shareholders in 2010-11 and 2011-12 and to see whether there was any violation of the provisions of the Securities and Exchange Board of India Act, 1992 (hereinafter referred to as '**SEBI Act**') and the Rules and Regulations made thereunder and possible violation of provision of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 (hereinafter referred to as '**PFUTP Regulations**').

SHOW CAUSE NOTICE

6. Consequent to the completion of examination, a common Show Cause Notice (hereinafter referred to as '**SCN**') dated January 05, 2018 was served on CBL, Dr. A.N. Singh (hereinafter referred to as '**Noticee No. 2**'), Mrs. Padma Singh (hereinafter referred to as '**Noticee No. 3**') and M/s Lakshmi Purna & Associates (hereinafter referred to as '**Noticee No. 4**') in the matter of Celestial Biolabs Limited to show cause as to why suitable actions/directions in terms of Sections 11(4) and 11B of the SEBI Act should not be initiated against them for the alleged violation of the provisions of Section 12A (b) of the SEBI Act and Regulation 3(c) and Regulations 4(1) and 4(2),(a),(e),(f),(k), and (r) of the PFUTP Regulations by Noticees No. 1 and 4 and Regulations 4(1)(a), (b), (c), (d), (e), (g) and (j) of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (hereinafter referred to as '**LODR Regulations**') by Noticees No. 2 and 3.
7. The facts as set out in the SCN are as follows:

- As per the annual reports, the company derives revenue from Formulations (which include herbal as well as allopathic formulations) and Bio-IT services. The sales of the company for the years 2010-11 and 2011-12 is as under:

(₹ in lakh)

S. No.	Sales	2010-11	2011-12
1	Formulations	1760.31	1324.35
2	Bio-IT services	762.01	734.53
	Total	2522.32	2058.88

- A summary of Profit and Loss accounts of the company for the financial years 2010-11 and 2011-12 is as under:

₹ (in lakh)	2011-12	2010-11
Sales- Formulations	1324.35	1760.31
Sales- Bio IT	734.53	762.01
Other Income	43.32	10.54
Total Revenue	2102.20	2532.86
Total Expenses	2073.79	2254.06
Profit/Loss Before Tax	28.41	278.80

- The company has shown sales to various companies which included some well-known brands such as Pfizer Limited, Glenmark Pharmaceuticals Limited, Merck Limited, Zandu Pharmaceuticals etc. as well as to various individuals.
- SEBI sought to obtain confirmation from various entities as to whether they have entered into any transactions in financial year 2010-11 or thereafter with CBL. These entities were requested to provide the nature of transaction, consideration paid etc. during the said period so as to confirm the genuineness of the sales so recorded by the Company.
- The entities to which communication made included some well-known brands

such as Pfizer Limited, Piramal Healthcare, Serum Institute of India, Themis Medicare Limited, Wockhardt Limited, Zandu Realty Limited, Narayana Institute for Advanced Research Pvt Ltd, Claris Life Sciences Limited and various other entities.

- These entities replied that after verification of books of accounts and audited financial statements, they have not come across any services being availed from CBL during the financial year 2010-11 and thereafter.
- A brief sample of the amount of sales as claimed by the company to various entities which have been denied by these entities are as follows :

S. No.	Entity Name	Sales claimed to be made by CBL in 2011-12 (in rupees)	Sales claimed to be made by CBL in 2010-11 (in rupees)
1	Claris Life Sciences Limited	8,60,000	23,25,000
2	Glenmark Pharmaceuticals Limited	1,95,000	32,75,000
3	Haffkine Pharmaceutical Corporation Ltd	34,75,000	28,50,000
4	Intas Bio Pharmaceuticals Ltd	22,80,000	30,00,000
5	Pfizer Limited	8,50,000	29,00,000
6	Serum Institute of India Limited	17,70,000	24,87,000
7	Themis Medicare Limited	8,25,000	17,00,000
8	Zandu Pharmaceuticals Limited	2,00,000	5,00,000
	Total	1,04,55,000	1,90,37,000

- The Managing Director of the company has also submitted that no funds were received by the company from the majority of invoices. The fact that no amount was received from the Bio-IT sales has been confirmed by the statutory auditors of the company, M/s Lakshmi Purna & Associates vide their certificate dated January 31, 2017 which indicates that the company showed fake sales amounting to ₹ 677 lakh in 2010-11 and ₹ 395 lakh in 2011-12.
- SEBI's examination found that the company resorted to creative accounting and

misstated its financial statements in order to present a rosy picture of its affairs by overstating its sales to the tune of ₹ 1072 lakh.

8. Thus, it was alleged in the SCN that Noticee no. 1 was involved in misstatement of accounts, adoption of dubious and inconsistent practices in drawing up accounts and employing devices to defraud the investors. It was further alleged that Noticee no.2 and Noticee no. 3, being the Non-Independent Directors of Noticee no. 1, were responsible for misstatement of accounts, adoption of dubious and inconsistent practices in drawing up accounts and employing devices to defraud the investors. Further, Noticee no. 4 being the auditor of the company during the financial years 2010-11 and 2011-12 was responsible for negligence in certification of accounts of listed company and lack of professional skepticism in audit.

REPLY

9. Noticee No. 1 vide its letter dated January 30, 2018 requested for additional 30 days' time to reply to the SCN as the company was pre occupied in the process of making OTS payments with SBI and identifying additional sources of investment in the company. Noticee No. 1 again vide its letter dated April 02, 2018 sought 30 days' time to reply to the SCN as Noticee No. 2 being the Chairman and Managing Director was hospitalized.
10. Noticee No 2 vide an undated letter received by SEBI on May 21, 2018 submitted as follows:
- In the years 2010-11 and 2011-12 clinical trial in India was just beginning. CBL had a strong presence with team of IT, mathematics, statistics biotechnology and bioinformatics. CBL was developing students in clinical data management offering training courses at its premises as well as client places. While offering training courses, CBL tried taking opportunity to get clinical data testing and analysis project with established pharma companies who were involved in developing new drugs for human and were conducting clinical trial. Its team leaders and team

members were providing many presentations and were involved in many discussions with client team and spent considerable time. Subject being new and in the absence of clear Govt. clinical regulations and service tax confusion, CBL could not secure the written contract but made considerable effort and spent many months of its professional's time on verbal engagement. Clinical data management involves collection of data, curation and obtain a pattern through algorithm. CBL was sure to get remuneration and that is why it made considerable effort for more than two years.

- Majority of pharma companies engaged in clinical trial are well connected through association. Unfortunately subject being new, keeping in view of complete confidentiality, lack of clear govt. regulations and service tax confusion, no company came forward to issue written contract and preferred to engage services on verbal contract. Parties were established and hence CBL continued to work to satisfy the client with result. Since drug development for human is a new phenomenon and have many research angles, every company interprets the result in its own way and ultimately, CBL became the victim as payments were not coming.
- CBL discussed the matter internally and also with auditors and decided to raise the invoice for the time spent by its team members and pursue client to make the payment. Service tax matters were not very clear for clinical data management and no client came forward to issue written contract.
- Dr. A.N. Singh was suffering with kidney ailment and was not involved in day to day operation. Senior manager and team dealt the whole subject. Dr. A.N. Singh was listening to team manager about the problems faced in subject. However, CBL was assured that clients are reputed and shall pay in due course of time.
- CBL did not make provision for bad debts pertaining to funds not received for

services and instead as doubtful receivable amount was treated as research oriented were booked in the head product development expenditure to the extent not written off and remaining amount was brought under debtor as we were hopeful to receive the amount. Similar arrangement of booking amount in product development expenditure to the extent not written off and debtor were adopted for the year 2011-12.

- The funds not received during the financial years 2010-11 and 2011-12 pertaining to clinical data testing and analysis project was properly accounted as product development expenditure to the extent not written off in asset side of books and accounts as per established procedure of ICAT. CBL has made such provisions of putting under head product development expenditure to the extent not written off from the year 2004- 2005 onwards and CBL has not created such heads only from 2010-11 and 2011-12. Companies involved in product development make such heads of product development expenditure in asset side of books and accounts and write off @ 10% every year. If the company gets desired result in product development, such amounts incurred becomes part of fixed asset. CBL's R&D activities are approved by DSIR, Ministry of Science and Technology and CBL has been writing off its product development expenditure @10% from 2004-2005 onwards. Kindly do not view such provisions as violation as it is done as per old established norms of accounting in research establishments.
- Service tax department on one hand claims that funds were received and on the other hand they referred the matter to SEBI that those entries are fictitious. The whole matter was dealt by a senior member of team and Promoter and only working director Dr. A.N. Singh has gone for renal transplant and was not attending office. When the funds were not received during the course of two years, CBL had stopped clinical data services and continued with formulations business. CBL did not initiate any legal or criminal charges against the senior member who

was responsible for clinical data testing project lapses as he left the country. CBL analysed the consequences of legal proceedings and it was again involving cost and effort and after Dr. A.N. Singh's recovery from illness, it was decided to concentrate on business rather than pursuing legal proceedings against a member who is not in the country.

- Invoices were made as per the time spent and also taking prevailing charges as per industry norm. All the invoices were in lakh as services rate is decided based on months and even rates in round figures of per month sum. In case of goods and quantities sold the invoices could be in decimal figure but in case of services and training pertaining to clinical data testing or for any services, the invoices shall always be in round figure. Kindly consider that invoices were raised by CBL were fully in order and also as per industry practices.
- CBL's research activities are recognised by DSIR (Ministry of Science and Technology). Being a DSIR recognised company, CBL is entitled to write off 100% research expenditure but auditor allowed only 10% as per previous history of written off. Income tax department view very negatively if 100% research expenditure is written off at a time. Auditor has followed guidelines of Indian accounting practices. Clinical data testing is a fully research based activity and when the results are not satisfactorily accepted and expenditure is incurred, such amount was booked under head product development expenditure to the extent not written off and subsequently was written off @ 10% every year.

11. CH L Purna Chandra Rao on behalf of Noticee No 4 vide his letter dated July 18, 2018 submitted as follows:

- In the years 2010-11 and 2011-12, clinical trial in India was just beginning. CBL had a strong presence with team of IT, mathematics, statistics biotechnology and bioinformatics. The company CBL was developing students in clinical data

management, offering training courses at their premises as well as client places. While offering training courses, they tried taking opportunity to get clinical data testing and analysis project with established Pharma companies who were involved in developing new drugs for humans and were conducting clinical trial.

- CBL team leaders and team members were providing many presentations and were involved in many discussions with client team and spent considerable time. Subject being new and in the absence of clear govt. clinical regulations, they could not secure the written contract but made considerable effort and spent many months of professionals' time on verbal engagement.
- Dr. A.N. Singh being the only working director was supposed to control the operation but he was suffering with serious ailment of kidney. He could not monitor the operation as he was not attending office. The company despite of their technical strength, could not market effectively and invited trouble. The company's drug clinical operation does not come under the purview of service tax. The company neither collected any service tax from its clients nor paid any tax to the Service Tax Department. However, unfortunately Service Tax Department treated the matter differently.
- Funds not received against sales of formulations and services were properly accounted as debtors. During the year 2011- 12, the company made a provision of ₹ 39 lakh for bad debts only in formulations sales as some goods were found damaged during transfer from C&F to distributors. We did not make provision for bad debts pertaining to funds not received for services and instead as doubtful receivable amount was treated as research oriented were booked in the head product development expenditure to the extent not written off and remaining amount was brought under debtor as the company was hopeful to receive the amount. Similar arrangement of booking amount in product development

expenditure to the extent not written off and debtor were adopted for the year 2011-12.

- Although debt was not recovered but company while interacting with different companies developed extensive know how. After discussing the whole matter with group of chartered accountants and auditors, it was decided that such know-how can be treated in balance sheet as intangible assets and shall be booked under head in product development expenditure. The company being in clinical operation can derive benefits of such know how in another 10 years and shall amortize the expenditure in 10 years @ 10% every year as per AS-26- ICAI guidelines. AS-26 says that self-generated know how can be treated as intangible assets in books of accounts and can be amortized in 10 years considering economic benefits.

HEARING

12. Vide hearing notice dated June 15, 2018, Noticees were granted an opportunity of hearing on July 24, 2018. In response to the hearing notice, Noticee No. 1 and Noticee No. 2 confirmed their attendance for the scheduled hearing vide its letter dated July 03, 2018 and vide his email dated July 17, 2018 respectively. Noticee No. 3 vide her letter dated July 03, 2018 had authorized Noticee No. 2 to appear for hearing on her behalf.
13. At the time of hearing, Noticee No. 2 appeared for the personal hearing on behalf of himself and the company and Ms. Padma Singh and made inter alia, the following oral submissions:
 - CBL was providing clinical data testing and analysis services from 2007-2008. From 2010-2011, the company started sending its teams to obtain project mandates from various clients. But the company did not receive any mandate.
 - The company raised invoice of sales based on the time and money spent in

obtaining mandates.

- The funds thus shown in the sales, which were not received were initially booked as "debtor" and carried forward and added to the expenditure under the head "product development expenditure". In the financial year 2010-2101, the company had booked Rs. 533 lakhs under the head of "debtor" which was later carried forward as "Product Development Expenditure".
- No restatement was carried out for the figures of sales shown in the preceding year after the unpaid amounts are carried forward as Product Development Expenditure.

Noticees were advised to provide in its written submissions, the relevant Accounting Standards used to book business development expenditure as "Sales". Further, the Noticees were advised to show the breakup of the values under the head of "debtors" into the categories of Formulation and Bio-IT Services. Noticees were also advised to confirm whether, after the values of "debtors" was carried forward as "Product Development Expenditure", any restatement was made in its financial statements to the figures showing "Sales".

During the personal hearing, Noticees were asked for its preliminary submissions to the query as to why the Promoters have been selling shares and have reduced their shareholding in the company from 37.31 % in the quarter ending June 2017 to 26.07% in the quarter ending June 2016.

On the queries raised at the time of personal hearing as to why the Promoters cannot be considered to have sold their shares at inflated prices as a result of the alleged misleading financial statements, Dr. A.N. Singh replied that the proceeds of the sale, were given to the Bank to service its loans taken. Further, he stated that unsecured loan of ₹ 4.07 crore was given to the company by the Promoters, largely from the proceeds of sale of shares.

The entities were advised to provide the full details of the unsecured loans, the

proceeds of sale of shares in the financial year 2017-2018 resulting in the fall in Promoter shareholding from 37.31% to 26.07%, and the details of the payments made to the Bank to repay loans, along with documentary evidence.

Further, the entities were asked to make preliminary submissions with regard to the decrease in the promoter shareholding from 38.81% in the quarter ending June 2015 to 35.16% in the quarter ending June 2016. The entities replied that the same was due to dilution of shareholding pursuant to a preferential allotment to one Mr. Mukesh Shah, who was known to one of the distributors of the company. The entities were advised to provide the details of the preferential allotment including price at which the allotment was made.

The entities were advised to file their written submission by August 10, 2018. The company was advised to submit the Board Resolution authorizing Dr. A.N. Singh to appear on its behalf, in the absence of which the present submissions will not be considered to have been made on behalf of the company.

Lakshmi Purna & Associates, Chartered Accountants, failed to appear for the personal hearing.

14. Pursuant to the hearing, CBL vide its letter dated August 10, 2018 submitted as follows:

- That our service contracts with other companies were on verbal engagement. "A contract is an agreement between two or more parties that creates enforceable rights and obligations. Enforceability is a matter of law. Contracts can be written, oral, or implied by an entity". Treating the verbal agreement as valid contract, the invoices were raised by the company based on description of the subject, man month rate agreed with mutual consent. The amount in invoices were discussed and agreed by parties depending on work requirement and qualification and experience of our team member.

- "Revenue recognition is mainly concerned with the timing of recognition of revenue in the statement of profit and loss of an enterprise. The accounting standard AS-9 issued by ICAI guidelines was followed to recognize the revenue in our books of accounts". Proportionate completion method was adopted to raise the invoices.
- "AS-9 Revenue Recognition: As per the AS-9 Revenue Recognition issued by ICAI, revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, rendering of services & from various other sources like interest, royalties & dividend."
- Acceptability of oral agreement under Indian Contract Act: On the validity of oral agreements while dealing with several cases, the courts recognized the acceptability of oral agreements once they were found to be fulfilling the essentials provided in Section 10. As we see in the case of *Alka Base vs. Parmatma Devi & Ors* [Civil Appeal No(s). 6197 of 2000], the Supreme Court by coming to the conclusion of the case observed that how oral agreements are valid. A sale agreement can be oral also and valid. It is not necessary that agreement should be written, what is more important is that it should be within the ambit of Section 10 of the Indian Contract Act. All oral and written agreements will be valid if they fulfill the conditions specified in Section 10.
- In our case, the services were offered after discussing the subject, payment terms etc. with the business entities. Thus, we are meeting the essentials of Section 10 of Indian Contract Act and recognized the revenue in our books of accounts at the time when respective invoices were raised on proportionate completion basis of work by following the guidelines as per accounting standard AS-9 issued by ICAI.

- Clinical services are an integral part of product development. The company has been booking the product development expenditure to the extent not written off in current asset head since 2005 as the company research and development services are recognized by DSIR (Department of Science and Industrial research in Ministry of Science and Technology).
- Promoter Director have sold 25 lakhs shares and brought the total funds in company as unsecured loan shown as unsecured loan from others. The unsecured loan amount reflected in last audited balance sheet is ₹ 4.27 crore. The funds were used to reduce outstanding term loan from bank given to the company. Promoters' shareholding shall be increased by issuing preferential shares as the amount has already been brought in the company. The Noticee enclosed the details of bank statements about the consideration received from promoters' shares sale and funds brought in the company. A copy of the audited balance sheet reflecting unsecured loan from others was also enclosed.

FINDINGS & CONSIDERATIONS

15. I have perused the SCN, replies, written submissions and other materials available on record. On perusal of the same, the following issues arise for consideration. Each issue is dealt with separately under different headings.

- (i) Whether CBL has misstated its accounts, adopted dubious and inconsistent practices in drawing up accounts and has employed devices to defraud investors as alleged in the SCN?
- (ii) If answer to issue No. 1 is in affirmative, who all are liable for misstatement of accounts, adoption of dubious and inconsistent practices in drawing up accounts and employing devices to defraud investors?
- (iii) Whether the Noticees have violated the provisions of SEBI Act read with PFUTP Regulations?

- (iv) Whether CBL, Dr. A.N. Singh and Ms. Padma Singh have violated provisions of LODR Regulations?
- (v) What directions, if any should be issued against the Noticees?

Issue No. 1 - *Whether CBL has misstated its accounts, adopted dubious and inconsistent practices in drawing up accounts and has employed devices to defraud investors as alleged in the SCN?*

16. I note that to arrive at a finding, the following two sub-issues needs to be addressed:

- i. Whether the accounts of the company were misstated by showing inflated sales figure in Bio-IT during the years 2010-11 and 2011-12 which also resulted in the profit figures and debtors of the company being overstated.
- ii. Assuming that sales figure in Bio-IT during the years 2010-11 and 2011-12 were representing the true state of affairs of the company as claimed by the company, whether, the said sales could be reclassified under Product Development Expenditure as they were intangible assets as per AS 26 of ICAI Guidelines.

A. Whether the accounts of the company were misstated by showing inflated sales figure in Bio-IT during the years 2010-11 and 2011-12 which also resulted in the profit figures and debtors of the company being overstated.

17. CBL has submitted that in the years 2010-11 and 2011-12 subject of clinical trial in India being new, keeping in view of complete confidentiality, lack of clear government regulations and service tax confusion, CBL could not secure the written contract but made considerable effort and spent many months of its professional's time on verbal engagement. Its team leaders and team members were providing many presentations and were involved in many discussions with client team and spent considerable time. CBL discussed the matter internally and also with auditors and decided to raise the invoice for the time spent by its team members and pursue client to make the payment.

18. I note from the material made available on record that CBL has shown sales to various companies which includes some well-known brands such as Pfizer Limited, Glenmark Pharmaceuticals Limited, Merck Limited, Zandu Pharmaceuticals etc. as well as to various individuals. When SEBI sought to obtain confirmation from various entities as to whether they have entered into any transactions in financial year 2010-11 or thereafter with CBL, these entities replied after verifying their books of accounts and audited financial statements that they have not come across any services being availed from CBL during the financial year 2010-11 and thereafter.
19. A brief sample of the amount of sales as claimed by CBL to various entities which have been denied by these entities are as follows:

S. No.	Entity Name	Sales claimed to be made by CBL in 2011-12 (in ₹)	Sales claimed to be made by CBL in 2010-11 (in ₹)
1	Claris Life Sciences Ltd.	8,60,000	23,25,000
2	Glenmark Pharmaceuticals Ltd.	1,95,000	32,75,000
3	Haffkine Pharmaceutical Corporation Ltd	34,75,000	28,50,000
4	Intas Bio Pharmaceuticals Ltd.	22,80,000	30,00,000
5	Pfizer Ltd.	8,50,000	29,00,000
6	Serum Institute of India Ltd.	17,70,000	24,87,000
7	Themis Medicare Ltd.	8,25,000	17,00,000
8	Zandu Pharmaceuticals Ltd.	2,00,000	5,00,000
	Total	1,04,55,000	1,90,37,000

20. CBL's submission that they were unable to secure a written contract / agreement from all the pharma companies to whom they have provided clinical trial services is not tenable. The work as per CBL's submission entailed collection of data, curation and obtaining a pattern through algorithm. As per CBL's submission, the work was confidential in nature. I note that the result of the work will be the intellectual property of the pharma company availing the services of CBL. It does not seem plausible that neither CBL nor the pharma company availing the services of CBL entered into a well-defined written agreement protecting their rights and interests.

It seems highly improbable that not one but all the pharma companies wanted to carry out such sensitive / confidential work without entering into a formal agreement or at least the nature and scope of work were reduced to writing. CBL has also not submitted any kind of correspondence, emails or letters with the pharma companies substantiating that CBL was working on some project with the pharma companies pursuant to the oral agreement. In other words, it is the claim of CBL that subsequent to the oral agreement, CBL had never during the entire tenure of the project, had any kind of written communication with the pharma companies. All the nuances and nitty gritty of the project were discussed without leaving a paper trail. This practice of not maintaining any kind of records for an ongoing project was followed not with one pharma company but uniformly with all the pharma companies. Further, even all the pharma companies used to communicate their requirements / queries orally only to CBL. The aforesaid when seen in the light of submission of pharma companies that they have not received any services from CBL, leads credence to the findings of the investigation that the work orders purportedly received by CBL related to clinical trials based on verbal agreements were in fact non – existent.

21. CBL has further submitted that its team leaders and team members were providing many presentations and were involved in many discussions with client team and spent considerable time. The company has not submitted any particulars about the presentations as to when and where and to whom these presentations were made or any correspondence with respect to the presentations with its clients. Further, the company has submitted that it has raised invoices for the time spent by its team members. However, it has not corroborated its submission with timesheets approved by its clients for the time billed to them. Thus, the aforesaid submissions of CBL are not acceptable. Even if it is assumed that CBL's employees have spent time in giving presentations and were involved in discussions with client team, the same are pre – sales Business Development activity, which is not billable.

22. CBL has submitted sample invoices raised for its clinical data testing services. However, CBL has not submitted any documentary proof for the invoices being sent to its clients via post or email. Similarly, no communication / follow up with the clients have been placed on record, requesting them to release the payment due to CBL. All the aforesaid circumstances leads to the conclusion that the invoices for Bio-IT sales made to pharma companies are not genuine and are for non-existent transactions.
23. In view of the above, it is concluded that CBL has failed to bring on record any documentary evidence substantiating its claim that it had entered into an oral agreement for clinical data management services with pharma companies. Therefore, it is held that the sales figure shown by CBL in its Annual Reports for the years 2010-11 and 2011-12 are not the correct representation of the Bio-IT sales made by the company.
24. The aforesaid finding, leads to another conclusion that, if there were no sales made in Bio-IT for clinical data testing project during the years 2010-11 and 2011-12, no money was owed by any pharma company to CBL for the same. Hence, the debtors and profits for CBL for its Bio-IT operations in clinical data testing, have also been overstated to that extent.

B. Assuming that sales figure in Bio-IT during the years 2010-11 and 2011-12 were representing the true state of affairs of the company as claimed by the company, whether, the said sales could be reclassified under Product Development Expenditure as they were intangible assets as per AS 26 of ICAI Guidelines.

The first perspective

25. Without prejudice to the conclusions arrived at preceding paragraphs, let me assume that submissions made by CBL with respect to its Bio-IT sales to pharma companies are *prima facie* acceptable. The company has submitted that the funds which were not received by it, were booked initially as debtor and carried forwarded and debtor

not realised were clubbed and added to the expenditure not written off under the head Product Development Expenditure. It is further submitted that the amount was written off @ 10% every year as per accounting policy. It is also stated that the same was reflected in the P&L Accounts of the company.

26. The aforesaid contention of the Noticee No. 1 is in contradiction with its earlier contention that it was providing services to its clients. As per the Annual Reports of 2010-11 and 2011-12, CBL has shown it under the heading “Sales – Bio- IT”. If it was R&D, then it should have been shown as such from the beginning. The company need not wait for the pharma companies to default on its obligations to reclassify the sale as R&D / Product Development Expenditure. It is noted from the certificate dated January 31, 2017 given by statutory auditors of the company, M/s Lakshmi Purna & Associates that no amount was received from the Bio-IT sales in clinical data testing for the financial years 2010-11 and 2011-12. Further, Noticee No 2 at the time of his deposition before SEBI has deposed that no money was received from the clinical data testing. It is observed that as per the prevalent accounting practice, if it becomes certain that the company is not going to receive amounts from its debtors then the amount should be provisioned / written off fully rather than reclassifying the amount under the head Product Development Expenditure. CBL had made such a provision for doubtful debts for ₹ 39 lakh for the year 2011-12 for its sales in formulations. Therefore, the action of the company to include the amount of debtors not received under Product Development Expenditure is also not in line with the prevalent accounting practice. Moreover, as admitted by the Noticees, no restatement was carried out for the figures of sales shown in the preceding years after the unpaid amounts were carried forward as Product Development Expenditure.

The second perspective

27. The company has submitted that doubtful debts were booked under Product Development Expenditure as it was towards the know-how derived from clinical

services. Noticee No. 4 has submitted that the company while interacting with different pharma companies developed extensive know how. After discussing the whole matter with group of chartered accountants and auditors, it was decided that such know-how can be treated in balance sheet as intangible assets and shall be booked under head in Product Development Expenditure. The submissions of the Noticees are not acceptable for the following reasons:

- i. Product development essentially entails creation of products with new or different characteristics that offer new or additional benefits to the customer. It may involve modification of an existing product or its presentation, or formulation of an entirely new product that satisfies a newly defined customer want or market niche. The Noticees have not demonstrated what was the know-how gained by the company during its sale process and the subsequent product developed based on that know how.

Further, AS 26 defines intangible assets as follows:

“6. An intangible asset is an identifiable non-monetary asset, without physical substance, held for use in the production or supply of goods or services, for rental to others, or for administrative purposes.”

As per para 20 of AS 26, an intangible asset should be recognised if, and only if: (a) it is probable that the future economic benefits that are attributable to the asset will flow to the enterprise; and (b) the cost of the asset can be measured reliably.

On the one hand the Noticee has not adduced any proof of the know-how. Therefore, the question of treating non-existing know-how as intangible asset does not arise. Assuming that such a know-how was in existence, the Noticees have also not shown on what basis the said know-how was considered to have future economic benefits for the company. On the contrary admittedly, the company has stopped clinical data services from the year 2012 onwards, questioning the aspect of future economic benefits for the company. Therefore, it

is difficult to treat the said know-how as “intangible asset”.

- ii. Assuming that CBL was providing clinical data management services to pharma companies which were involved in developing new drugs for humans. The cost, if any, incurred for R&D by CBL would be for developing the tools for clinical data management but once it starts selling its services for clinical data management to various pharma companies, the expenditure incurred towards selling the services can no longer be classified as R&D expenditure. Even, assuming that there was product development in the form of clinical data management tools, simultaneously with the selling process, in the form of intangible asset, the entire proceeds of sale can never be considered as product development costs resulting into intangible asset, as the particular sales figure also reflects the compensation paid by pharma companies for the services availed by them from Noticee No. 1.

28. There can therefore be no hesitation in concluding, that based on both the perspectives, even if there were sales in clinical data testing by CBL, it could not have, reclassified the purported bad debts under Product Development Expenditure. The company instead of expensing the bad debt out, capitalized it by categorising it as intangible assets.

29. In light of the aforesaid conclusions, it is held that the company has resorted to the following mechanism to present a rosy picture of its financials:

- Book sales to various parties fictitiously and thereby show fictitious growth in top line/sales. Consequently the debtors and profits of the company were also overstated.
- Claim that the various parties to whom the sales were made are unable to make the payment.
- Do not write off the bad debt or make any provisions for doubtful debts. Instead, carry the amount of such debtors into Product Development Expenditure to hide the fabrication in sales made by it.

30. In view of the same, it is concluded that in the absence of any documentary evidence for the sale of clinical data management services by the company to pharma companies, it is held that sales figure of Bio-IT in that regard were overstated by ₹ 677 lakh in 2010-11 and ₹ 395 lakh in 2011-12. Consequently the debtors and profits of the company were also overstated. It is further concluded that CBL has misstated its accounts, adopted dubious and inconsistent practices in drawing up accounts and has employed devices to defraud investors by first claiming that pharma companies have bought their services, then claimed that they have defaulted in their obligations and finally reclassifying the purported bad debts under Product Development Expenditure.

Issue No. 2- *If answer to Issue No. 1 is in affirmative, who all are liable for misstatement of accounts, adoption of dubious and inconsistent practices in drawing up accounts and employing devices to defraud investors?*

31. It is noted from Annual Reports for the years 2010-11 and 2011-12 that during the said period, Dr. A.N. Singh was the Managing Director of the company and Ms. Padma Singh was the Director of the company. Dr. A.N. Singh has submitted that he was suffering from kidney transplant and was not involved in day to day operations. The Noticee has not submitted any documentary proof / medical records to substantiate his claim that he was away from the affairs of the company during the period of 2010-12. Even assuming that he was away from the affairs of the company, he being the controlling Promoter of the company, holding along with his family members 38.06% for year ending March, 2012, there is no evidence that some other person was appointed as a Managing Director in his absence. Moreover, it is noted from CBL's submission that the team manager use to communicate with Dr. A.N. Singh with respect to the problems faced by the company in Bio-IT sales. Further, as per his deposition also, he was being provided with the information regarding clinical data testing. Moreover, apart from being the signatory to the Annual Reports for the years 2010-11 and 2011-12, it is noted from the extracts of the Minutes of the Board

of Directors meeting held on February 03, 2012 that the same was signed by him. All the aforesaid circumstances leads to the conclusion that Dr. A.N. Singh was involved in the affairs of the company during the period 2010-12.

32. It is noted from the material made available on record that Ms. Padma Singh is the wife of Dr. A.N. Singh. Further, she is part of the Promoter Group wherein she along with her family members was holding 38.06% for the year ending March, 2012. Moreover, she was also on the Board of Directors of the company as a Director. In view of the aforesaid, it is concluded that Ms. Padma Singh being the part of the management of the company was involved in the affairs of the company during the period 2010-12. Further, the same as well as other allegations made against her in the SCN has also not being denied by her.

33. At this juncture, I would like to refer to the order of Hon'ble Supreme Court of India in the matter of *N Narayanan Vs. Adjudicating Officer, Sebi* decided on April 26, 2013. The Apex Court in the said matter observed as follows:

"32. Responsibility is cast on the Directors to prepare the annual records and reports and those accounts should reflect 'a true and fair view'. The overriding obligation of the Directors is to approve the accounts only if they are satisfied that they give true and fair view of the profits or loss for the relevant period and the correct financial position of the company.

33. Company though a legal entity cannot act by itself, it can act only through its Directors. They are expected to exercise their power on behalf of the company with utmost care, skill and diligence. This Court while describing what is the duty of a Director of a company held in Official Liquidator v. P.A. Tendolkar (1973) 1 SCC 602 that a Director may be shown to be placed and to have been so closely and so long associated personally with the management of the company that he will be deemed to be not merely cognizant of but liable for fraud in the conduct of business of the company even though no specific act of dishonesty is provide against him personally. He cannot

shut his eyes to what must be obvious to everyone who examines the affairs of the company even superficially.

...

Directors of the companies, especially of the listed companies, have access to inside knowledge, such as, financial position of the company, dividend rates, annual accounts etc. Directors are expected to exercise the powers for the purposes for which they are conferred. Sometimes they may misuse their powers for their personal gain and makes false representations to the public for unlawful gain.

..."

34. It has been concluded in preceding paragraphs that there was no evidence of sale of clinical data management services by the company to pharma companies. Such non-existent transactions enabled the company to project inflated figures of the company's revenue, profits and receivables. As noted from the Apex Court order, it is the responsibility of the Directors to prepare the Annual Report so that they reflect "a true and fair view". In the extant matter, Dr. A.N. Singh and Ms. Padma Singh being the Directors of the company have failed in their duty to exercise due care and diligence and were part of the deceptive device / scheme to fabricate the sales figures in Bio-IT pertaining to clinical data testing and making false disclosures. Therefore, it is held that that Dr. A.N. Singh and Ms. Padma Singh are liable for misstatement of accounts, have adopted dubious and inconsistent practices in drawing up accounts and have also employed devices to defraud investors.

35. Noticee No. 4 was the statutory auditor of the company during the period 2010-12. Being the statutory auditor, Noticee No. 4 is responsible for auditing the company's financial statements and forming an opinion as to their truth and fairness. The role played by Noticee No. 4 can be broadly classified under two categories:

- i. Certifying the sales figure in Bio-IT in the Annual Reports of 2010-11 and 2011-12.

- ii. Reclassifying the purported bad debts as Product Development Expenditure.

Certification of sales figure

36. It is noted from the Annual Reports that company has shown Bio-IT sales as at March 31, 2010 as ₹ 706 lakh, as at March 31, 2011 as ₹ 762.01 lakh and as at March 31, 2012 as ₹ 734.53 lakh. In the absence of any written agreement from any of the pharma companies coupled with the fact that the company was claiming that the pharma companies are defaulting in paying its dues, the same should have raised red flags for the auditor. However, the facts in the matter indicate that the auditor neither resorted to any independent verification nor the auditor verified the information from the other parties i.e. pharma companies. By accepting the information provided by the company at face value and performing a perfunctory job, the auditor has failed to live upto the expectations of the shareholders. Thus, the auditor has failed to follow the minimum standards of diligence and care as expected from a statutory auditor.
37. The auditor has merely accorded its concurrence to the invoices produced by the company. By accepting the invoices on its face value, the auditor was negligent and has shown lack of professional skepticism in auditing the accounts of the company. The auditors by adopting alternative procedures should have checked the source and genuineness of the invoices, particularly in the absence of any documentation whatsoever in the form of purchase order or a letter of intent or even an email confirmation from pharma companies. Unfortunately, this exercise was not carried out in a meaningful manner to check the veracity of sales figures.
38. It was brought to the notice of the auditor that pharma companies are defaulting on their purported dues. Thus, the pharma companies had become the debtors of the company. Noticee No. 4 being the auditor had the benefit of conducting a check, by way of sample, large or small as per its judgment with respect to the debtors of the company. The auditor could have sent confirmation letters to the persons claimed as

debtors by Noticee No 1, which would have helped the auditor in ascertaining whether such transactions were only paper transactions or they were genuine transactions with CBL. This would have been indicative of the professional skepticism required on the part of the auditor and the diligence with which the work was undertaken. However, this was not done.

Reclassification of the purported bad debts as Product Development Expenditure

39. It has been submitted by the Noticee No. 4 that as the company was unable to recover its dues from the pharma companies, the said amount was booked under the head in Product Development Expenditure. As stated in preceding paragraphs, as per the prevalent accounting practice, if it becomes certain that the company is not going to receive amounts from its debtors then the amount should be written off completely. While, AS-26 of ICAI Guidelines are applicable to intangible assets and the expenditure incurred can be amortized in 10 years, in the instant matter, the company had initially stated that it had entered into sales transactions with pharma companies and later wanted to classify the entire sales transactions in clinical data testing under R&D / Product Development Expenditure. The auditor should have exercised his professional skepticism to see through the actions of the company, as the company was claiming that not one but all the pharma companies are defaulting in their dues. The auditor also has not placed on record any material or parameters based on which an opinion was formed by the auditor that know-how was generated in the sale transaction and the future economic benefit of the purported know-how would have flown to the company, which is one of the essential ingredient of being classified as an intangible asset. Thus, the provisions of AS 26 were inappropriately used by the auditor to reflect non-existent and non-genuine assets of CBL within the company's books by design and not as an oversight. It is noted from the material made available on record that the company and the auditor have admitted that the whole matter i.e., treating the unrealised consideration as know-how under the head Product Development Expenditure, was discussed with a group of chartered

accountants and auditors before the same was reflected in company's books.

40. Here, I would like to quote the observations of Hon'ble High Court of Andhra Pradesh in the matter of *The Institute Of Chartered Accountants of India Vs. Shri Mukesh Gang, Chartered* decided on September 26, 2016 wherein the Court observed as follows:

"The Chartered Accountant is a professional whose expertise in accountancy is acknowledged. He is a member of an expert body and of a premier institute in India. The certificate issued by an Auditor has its own impact on the public at large, as it is largely on the basis of this certificate that the general public subscribe to the shares of the company. Reckless certification by an Auditor, which has resulted in the public being misled into subscribing to the shares of the company in the public issue, would undoubtedly amount to gross negligence. Large sections of society rely on the certification by the Chartered Accountants for taking many vital decisions. It is imperative that utmost care and caution is exercised in issuing such certificates, and the objectivity, integrity, reliability and credibility of the information therein is ensured. Of late, several instances have come to light where, due to the erroneous/ambiguous advice tendered by Chartered Accountants, borrowal accounts have had to face quick mortality resulting in huge losses for banks and financial institutions. To ensure public faith and protect gullible small investors from being cheated of their life savings, the Institute should ensure that its members possess competence of a high order, their character is above board, and their integrity beyond reproach. Chartered Accountants are responsible to the public for their actions, as heavy reliance is placed on their credibility by the general public consisting of investors, banks, financial institutions, governments etc. The Chartered Accountants duty is not merely to his client, but extends to various segments of society, more particularly in the commercial field, on whose expertise, integrity and impartiality they rely on in taking various decisions."

41. In *Registrar of Companies, Bombay Vs. P M Hegde* decided on April 30, 1954 the Hon'ble High Court of Madras, considered the question whether the auditor's job is to verify the figures set out in the balance sheet tally with the figures found in the

accounts of the Bank. The Hon'ble High Court therein had referred to the following cases, before holding that the auditor has not discharged the duties which lay on him as an auditor:

Leeds Estate, Building & Investment Co. v. Shepherd, (1887) 36 Ch D 787 at p. 802. Stirling J. observed thus:

"It was in my opinion the duty of the auditor not to confine himself merely to the task of verifying the arithmetical accuracy of the balance sheet, but to inquire into its substantial accuracy, and to ascertain that it contained the particulars specified in the articles of association (and consequently a proper income and expenditure account) and was properly drawn up, so as to contain a true and correct representation of the state of the company's affairs."

In re London and General Bank (No. 2), 1895-2 Ch 673 (D) at pp. 682-3 Lindley L. J. after stating that the business of the auditor is to ascertain and state the true financial position of the company at the time of the audit, and that his duty is confined to that, asked the question, "How is he to ascertain that position?" and answers it thus:

"The answer is, by examining the books of the company, But he does not discharge his duty by doing this without inquiry and without taking any trouble to see that the books themselves show the company's true position. He must take reasonable care to ascertain that they do so. Unless he does this his audit would be worse than an idle farce.....But his first duty is to examine the books, not merely for the purpose of ascertaining what they do show, but also for the purpose of satisfying himself that they show the true financial position of the company."

42. Taking support of aforesaid decisions and findings arrived at preceding paragraphs, I find that there has not only been a total abdication by the auditor of its duty to follow the minimum standards of diligence and care expected from a statutory auditor. The records reflect that the attitude of professional skepticism was missing for two years. The auditor has not taken reasonable care to ascertain that the

contents of the balance sheet and P&L statement of the company were substantially accurate and that it contains a correct representation of the state of the company's affairs.

43. In view of the above, it is held that M/s Lakshmi Purna & Associates being the statutory auditor of CBL was not cautious and careful while certifying the Annual Accounts of CBL but was rather negligent and lacked professional skepticism in its audit. Such reckless certification of Annual Reports by the Noticee No. 4 has resulted in not only the shareholders but also the public being misled about the sales performance of the company in Bio-IT, consequently its debtors and profit figures were also overstated and overall state of the company's affairs which undoubtedly amounts to gross negligence. Further, the omission on the part of auditor to do independent verification of sales figure in Bio-IT after being made aware by the company of the default in payments by the pharma companies, indicates that the omission was by design and not an oversight. Also, before classifying the purported bad debts under Product Development Expenditure by treating them as intangible assets, the matter was discussed by the auditor with the company and other chartered accountants.

Issue No. 3- Whether the Noticees have violated the provisions of SEBI Act read with PFUTP Regulations?

44. Before proceeding further, it will be appropriate to refer to the relevant provisions of SEBI Act and PFUTP Regulations, which read as under:

SEBI Act, 1992

Prohibition of manipulative and deceptive devices, insider trading and substantial acquisition of securities or control

Section 12A: No person shall directly or indirectly:

...

(b) employ any device, scheme or artifice to defraud in connection with issue or dealing in securities which are listed or proposed to be listed on a recognised stock exchange;

PFUTP Regulations

Regulation 3. Prohibition of certain dealings in securities

No person shall directly or indirectly-

...

(c) employ any device, scheme or artifice to defraud in connection with dealing in or issue of securities which are listed or proposed to be listed on a recognized stock exchange;

Regulation 4. Prohibition of manipulative, fraudulent and unfair trade practices

(1) Without prejudice to the provisions of regulation 3, no person shall indulge in a fraudulent or an unfair trade practice in securities.

(2) Dealing in securities shall be deemed to be a fraudulent or an unfair trade practice if it involves fraud and may include all or any of the following, namely:--

(a) indulging in an act which creates false or misleading appearance of trading in the securities market;

(e) any act or omission amounting to manipulation of the price of a security;

(f) publishing or causing to publish or reporting or causing to report by a person

dealing in securities any information which is not true or which he does not believe to be true prior to or in the course of dealing in securities;

...

(k) an advertisement that is misleading or that contains information in a distorted manner and which may influence the decision of the investors;

...

(r) planting false or misleading news which may induce sale or purchase of securities;

45. The object and purpose of the abovementioned statutory provisions are to curb market manipulation. Palmer's Company Law, 25th Edition (2010), Volume 2 at page 11097 states: *"Market manipulation is normally regarded as the "unwarranted" interference in the operation of ordinary market forces of supply and demand and thus undermines the "integrity" and efficiency of the market."*

46. Hon'ble Supreme Court of India in the matter of *N Narayanan Vs. Adjudicating Officer, Sebi* decided on April 26, 2013 while dealing with the concept of market abuse in securities market has observed as follows:

"Prevention of market abuse and preservation of market integrity is the hallmark of Securities Law. Section 12A read with Regulations 3 and 4 of the Regulations 2003 essentially intended to preserve 'market integrity' and to prevent 'Market abuse'. The object of the SEBI Act is to protect the interest of investors in securities and to promote the development and to regulate the securities market, so as to promote orderly, healthy growth of securities market and to promote investors protection. Securities market is based on free and open access to information, the integrity of the market is predicated on the quality and the manner on which it is made available to market. 'Market abuse' impairs economic growth and erodes investor's confidence. Market abuse refers to the use of manipulative and deceptive devices, giving out incorrect or misleading information, so as to encourage investors to jump into conclusions, on wrong premises, which is known to be wrong to the abusers. The statutory provisions mentioned earlier deal with the situations where a person, who deals in securities, takes advantage of the impact of an action, may be manipulative, on the anticipated impact

on the market resulting in the “creation of artificiality”. The same can be achieved by inflating the company’s revenue, profits, security deposits and receivables, resulting in price rise of scrip of the company. Investors are then lured to make their “investment decisions” on those manipulated inflated results, using the above devices which will amount to market abuse.”

47. Further, fraud has been defined under Section 2 (1) (c) of PFUTP Regulations which reads as under:-

“fraud” includes any act, expression, omission or concealment committed whether in a deceitful manner or not by a person or by any other person with his connivance or by his agent while dealing in securities in order to induce another person or his agent to deal in securities, whether or not there is any wrongful gain or avoidance of any loss, and shall also include--

(1) a knowing misrepresentation of the truth or concealment of material fact in order that another person may act to his detriment;

(2) a suggestion as to a fact which is not true by one who does not believe it to be true;

(3) an active concealment of a fact by a person having knowledge or belief of the fact;

(4) a promise made without any intention of performing it;

(5) a representation made in a reckless and careless manner whether it be true or false;

(6) any such act or omission as any other law specifically declares to be fraudulent;

(7) deceptive behavior by a person depriving another of informed consent or full participation;

(8) a false statement made without reasonable ground for believing it to be true;

(9) the act of an issuer of securities giving out misinformation that affects the market

price of the security, resulting in investors being effectively misled even though they did not rely on the statement itself or anything derived from it other than the market price.

And “fraudulent” shall be construed accordingly;

48. The Hon'ble Securities Appellate Tribunal in the matter of *V. Natarajan Vs. SEBI*, Appeal No. 104 of 2011, wherein it observed -

"... We are satisfied that the provisions of Regulations 3 and 4 of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003, were violated. These regulations, among others ... prohibit persons from engaging in any act, practice, course of business which operates or would operate as fraud or deceit upon any person in connection with any dealing in or issue of securities that are listed on stock exchanges.

... A basic premise that underlies the integrity of securities market is that persons connected with securities market conform to standards of transparency, good governance and ethical behaviour prescribed in securities laws and do not resort to fraudulent activities."

49. On facts, it has been clearly found that the company has employed deceptive devices by projecting inflated sales in Bio-IT and had adopted dubious and inconsistent practices in drawing up accounts for manipulating the financial results of the company to present a rosy picture to its shareholders and to the public at large. Company though a legal entity, cannot act by itself and would not have been able to draw up this elaborate scheme without its Directors and statutory auditor being part of the manipulative and deceptive device. Dr. A.N. Singh, Ms. Padma Singh and M/s Lakshmi Purna & Associates by playing their respective roles in this elaborate scheme, adopted a fraudulent device and artifice to defraud the genuine shareholders of the company by first falsely portraying sales transactions with pharma companies in Bio-IT services and then by treating the purported bad debts

under the heading Product Development Expenditure. Noticees have admitted that after discussing the whole matter with chartered accountants and auditors i.e. pharma companies defaulting on their dues to CBL, it was decided to treat the unrealized consideration under the head of Product Development Expenditure. This shows that the Noticees were part of the deceptive device / plan to present a rosy picture of the affairs of the company by overstating its sales and then restored to creative accounting to camouflage the non-existent transactions in the books of the company.

50. Upon considering all facts and circumstances in totality, I find that such acts and omissions were with deliberate design of the Noticees as part of their manipulative and deceptive device, plan or artifice. When the picture is looked at in totality, what is unfolding is a fraud perpetuated on the market / investors. Such acts of serious irregularities threaten the market integrity and orderly development of the market and calls for regulatory intervention to protect the interest of investors. I therefore, find that the CBL, Dr. A.N. Singh, Ms. Padma Singh and M/s Lakshmi Purna & Associates have violated Section 12A (b) of SEBI Act and Regulation 3(c) and Regulations 4(1) and 4(2),(a),(e),(f),(k), and (r) of the PFUTP Regulations.

Issue No. 4 - Whether CBL, Dr. A.N. Singh and Ms. Padma Singh have violated provisions of LODR Regulations as alleged in the SCN?

51. The provisions of LODR regulations alleged to have been violated by CBL, Dr. A.N. Singh and Ms. Padma Singh are reproduced below:

LODR Regulations

Principles governing disclosures and obligations.

4.(1) The listed entity which has listed securities shall make disclosures and abide by its obligations under these regulations, in accordance with the following principles:

(a) Information shall be prepared and disclosed in accordance with applicable standards of accounting and financial disclosure.

(b) The listed entity shall implement the prescribed accounting standards in letter and spirit in the preparation of financial statements taking into consideration the interest of all stakeholders and shall also ensure that the annual audit is conducted by an independent, competent and qualified auditor.

(c) The listed entity shall refrain from misrepresentation and ensure that the information provided to recognised stock exchange(s) and investors is not misleading.

(d) The listed entity shall provide adequate and timely information to recognised stock exchange(s) and investors.

(e) The listed entity shall ensure that disseminations made under provisions of these regulations and circulars made thereunder, are adequate, accurate, explicit, timely and presented in a simple language.

...

(g) The listed entity shall abide by all the provisions of the applicable laws including the securities laws and also such other guidelines as may be issued from time to time by the Board and the recognised stock exchange(s) in this regard and as may be applicable.

...

(j) Periodic filings, reports, statements, documents and information reports shall contain information that shall enable investors to track the performance of a listed entity over regular intervals of time and shall provide sufficient information to enable investors to assess the current status of a listed entity.

52. The above statutory provisions deal with the timely and accurate disclosure of financial statements prepared as per the applicable accounting standard to the stock

exchange so as to enable investors to assess and track the performance of a listed company.

53. Here, I would like to quote the order of Hon'ble Securities Appellate Tribunal in the matter of *Mr. Ankur Chaturvedi Vs. SEBI* decided on August 04, 2015, wherein the Tribunal observed as follows:

"...the entire securities market stands on disclosure based regime and accurate and timely disclosures are fundamental in maintaining the integrity of the securities market. ..."

54. It has been held in preceding paragraph that the company has shown fake sales amounting to ₹ 677 lakh in 2010-11 and ₹ 395 lakh in 2011-12 and the same was disclosed in its Annual Reports. Therefore, it is held that the CBL has violated Regulations 4(1)(a), (b), (c), (d), (e), (g) and (j) of LODR Regulations.

55. As per Regulation 4 (2) (f) (ii) (7) of LODR Regulations, it is the responsibility of the Board of Directors to ensure the integrity of the listed entity's accounting and financial reporting systems. Further, as per Regulation 4 (2) (f) (ii) (8) of LODR Regulations it is also the responsibility of the Board of Directors to oversee the process of disclosure and communications.

56. Further, in addition to the above provisions of LODR Regulations to determine whether the controlling Promoters – Directors are liable for the violations of LODR Regulations as mentioned at paragraph 51, it would be appropriate to consider the doctrine of lifting of corporate veil. Regarding the requirement of lifting the corporate veil, I note that the Hon'ble Securities Appellate Tribunal had an occasion to deal with the said aspect in detail in the order dated July 28, 2017 passed in *Sahara Asset Management Company P. Ltd and other Vs. SEBI* (Appeal No. 428 of 2015) (hereinafter referred to as "**Sahara Judgment**"). In the said appeal it was argued that under the Mutual Fund Regulations, there is a requirement for the sponsor to be a fit and proper person. It was argued that the requirement of being fit and proper

person is on the applicant company who acts as the sponsor and the said requirement is not its Promoters under Mutual Fund Regulations. It was further argued, the sponsor is a separate legal entity as distinct from its shareholders and therefore just because one of the 8 shareholders is allegedly not a fit and proper person it cannot result in the sponsor being declared as not a fit and proper person. The Hon'ble Tribunal also recorded the argument that a company is a separate juristic person distinct from the promoters / directors; corporate veil cannot be lifted except in matters of fraud etc.

57. After dealing with the arguments, the Hon'ble SAT held that *"In the securities market, SEBI Act empowers SEBI to take actions in the interest of protecting the interests of the investors and hence lifting the corporate veil to the extent to identify who controls a regulated entity cannot be faulted"*.

58. On perusal of the above judgment, I note that the requirement of being fit and proper was, inter alia, on the Sponsor Company which in that case was a corporate entity. The Hon'ble SAT pierced the veil of the corporate entity and looked into the controlling shareholder (Promoter) and applied the legal requirement on the controlling shareholder. In the case in hand the obligation under LODR Regulations have been imposed on the listed entity. The said requirements in question here though were imposed on the corporate entity, the fact is that the listed company is not in compliance of the said requirements in question, since the directors who also happen to be controlling shareholders have committed fraud as elaborated earlier. In view of the fraud, this case is a fit case to lift the corporate veil and see the true state of facts for non-compliance of LODR Regulations. Once the corporate veil is pierced, the failure of non-compliance of the LODR Regulations in question would take the character of failure by the Promoter/Directors. Therefore, I consider this as a fit case where it should be considered that the Promoter/Directors by virtue of their fraud have not performed the LODR obligations in question and they should be equally liable for non-compliance of LODR obligations in question along with the

Company. The contrary view would only enable the controlling promoters/directors to take the mask of corporate personality and claim that it is not their responsibility as they are distinct from the Corporate entity, the view of which will only bring to reality the fear expressed by the Hon'ble SAT in the following words in Sahara judgment. "Without such a power SEBI will be a mute spectator to many of the corporate misdeeds which may jeopardize the interests of investors. Given the mandate of SEBI to protect the interests of the investors in the securities market SEBI is statutorily empowered to lift the corporate veil and find out the truth whenever interests of the investors are affected or likely to be affected."

59. It has already been held that the company has falsified its books of accounts which leads to the conclusion that Dr. A.N. Singh and Ms. Padma Singh have violated Regulations 4(1)(a), (b), (c), (d), (e), (g) and (j) of LODR Regulations read with Regulation 4 (2) (f) (ii) (7) and (8) of LODR Regulations.

60. In addition to the above provisions, I would also like to refer to the Section 27 of SEBI Act which states as follows:

SEBI Act

Offences by companies.

27.(1) Where an offence under this Act has been committed by a company, every person who at the time the offence was committed was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly:

Provided that nothing contained in this sub-section shall render any such person liable to any punishment provided in this Act, if he proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence.

(2) Notwithstanding anything contained in sub-section (1), where an offence under this Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

61. In this context reference may be made to Section 68 of FERA which is *pari materia* to Section 27 of SEBI Act. The Hon'ble Supreme Court of India while dealing with Section 68 of Foreign Exchange Regulation Act, 1973 in *Standard Chartered Bank Vs Directorate Of Enforcement* in its judgment dated February 24, 2006 observed as follows:

"The word 'offence' is not defined in the Act. According to Concise Oxford English Dictionary, it means, 'an act or instance of offending'. Offend means, 'commit an illegal act' and illegal means, 'contrary to or forbidden by law'. According to New Shorter Oxford English Dictionary, an offence is "a breach of law, rules, duty, propriety, etiquette, an illegal act, a transgression, sin, wrong, misdemeanour, misdeed, fault." Thus, an offence only means the commission of an act contrary to or forbidden by law. It is not confined to the commission of a crime alone. It is an act committed against law or omitted where the law requires it and punishable by it. In its legal signification, an offence is the transgression of a law; a breach of the laws established for the protection of the public as distinguished from an infringement of mere private rights; a punishable violation of law, a crime, the doing that which a penal law forbids to be done or omitting to do what it commands (see P. Ramanatha Aiyar's Advanced Law Lexicon, 3rd Edn, 2005 page 3302). This Court in Depot Manager, Andhra Pradesh State Road Transport Corporation Vs. Mohd. Yousuf Miya [(1997) 2 SCC 699] stated that the word 'offence' generally implies infringement of a public duty, as distinguished from mere private rights punishable under criminal law. In Brown v. Allweather Mechanical co. [(1954) 2 QB 443], it was described as "a failure to do something prescribed by a statute may be

described as an offence, though no criminal sanction is imposed but merely a pecuniary sanction recoverable as a civil debt." (underlining supplied).

62. In light of the aforesaid Apex Court order and Section 27 of SEBI Act being *pari materia* to Section 68 of Foreign Exchange Regulation Act, 1973, it is just and fair to apply the same parameters to Section 27 of SEBI Act while interpreting the expression 'offence' for assigning liability on the Directors of the company.

63. It has been held in preceding paragraphs that Dr. A.N. Singh and Ms. Padma Singh being the Directors of the company have failed in their duty to exercise due care and diligence and were part of the deceptive device / scheme to fabricate the sales figures in Bio-IT and making false disclosures. Hence, it is held that they have violated Regulations 4(1)(a), (b), (c), (d), (e), (g) and (j) of LODR Regulations.

Issue No. 5- What directions, if any should be issued against the Noticees?

64. In view of the findings above, I am of the considered view that under Sections 11B and 11(4) of the SEBI Act for the violation of provisions of Section 12A (b) of SEBI Act, Regulations 3 (c), 4(1), (2)(a), (e), (f), (k) and (r) of PFUTP Regulations and Regulations 4(1)(a), (b), (c), (d), (e), (g) and (j) of LODR Regulations, CBL, Dr. A.N. Singh and Ms. Padma Singh should be restrained for a suitable period of time. Further, for the violation of provisions of Section 12A (b) of SEBI Act and Regulations 3 (c), 4(1), (2)(a), (e), (f), (k) and (r) of PFUTP Regulations, M/s. Lakshmi Purna & Associates should be banned from certification of listed entities for a suitable period of time.

ORDER

65. In the facts and circumstances of the case, I, in exercise of the powers conferred upon me under Sections 11, 11 (4) (b) and 11B read with Section 19 of the Securities and Exchange Board of India Act, 1992, hereby issue following directions:

a) CBL, Dr. A.N. Singh and Ms. Padma Singh shall not buy, sell or otherwise deal in

the securities market in any manner whatsoever or access the securities market, directly or indirectly, for a period of ten years from the date of this order. Further, Dr. A.N. Singh and Ms. Padma Singh are also restrained from associating themselves with any listed public company and any public company which intends to raise money from the public, or any intermediary registered with SEBI for a period of ten years from the date of this order.

b) Lakshmi Purna & Associates shall not directly or indirectly issue any certificate of audit of listed companies, compliance of obligations of listed companies and intermediaries registered with SEBI and the requirements under SEBI Act, Securities Contracts (Regulation) Act, 1956, Depositories Act, 1996, those provisions of the Companies Act 2013 which are administered by SEBI under Section 24 thereof, the Rules, Regulations and Guidelines made under those Acts which are administered by SEBI for a period of five years.

c) Listed companies and intermediaries registered with SEBI shall not engage Lakshmi Purna & Associates, for issuing any certificate with respect to compliance of statutory obligations which SEBI is competent to administer and enforce, under various laws for a period of five years.

66. I find that in the SCN dated January 05, 2018, the charge of violation of provisions of LODR Regulations against the company was inadvertently left out. In view of the same, this order will take effect as final order against the company with respect to the findings under LODR Regulations on the expiry of 30 days from the date of service of this order, unless the company, within such period of 30 days from the date of service of this order files its objections. Till that time the directions against the company will operate as interim directions. If no objections are filed, the findings under LODR Regulations qua the company in this order will come into effect. If objections are filed, then the directions passed herein against the company shall be made applicable subject to the determination on the objections. Till the

determination of the objections, the directions against the company will operate as interim directions.

67. Similarly, I note that in the SCN dated January 05, 2018, the charge of violation of provisions of SEBI Act and PFUTP Regulations against Dr. A.N. Singh and Ms. Padma Singh were inadvertently left out. In view of the same, this order will take effect as final order against the Dr. A.N. Singh and Ms. Padma Singh with respect to the findings under SEBI Act and PFUTP Regulations on the expiry of 30 days from the date of service of this order, unless Dr. A.N. Singh and Ms. Padma Singh, within such period of 30 days from the date of service of this order file their objections. Till that time the directions against Dr. A.N. Singh and Ms. Padma Singh will operate as interim directions. If no objections are filed, the findings under SEBI Act and PFUTP Regulations qua Dr. A.N. Singh and Ms. Padma Singh in this order will come into effect. If objections are filed, then the directions passed herein against Dr. A.N. Singh and Ms. Padma Singh shall be made applicable subject to the determination on the objections. Till the determination of the objections, the directions against the Dr. A.N. Singh and Ms. Padma Singh will operate as interim directions.

68. Subject to paragraphs 66 and 67, the order shall come into force with immediate effect.

69. A copy of this order shall be served upon all the Noticees, Stock Exchanges and Depositories for necessary action and compliance with the above directions.

70. This order is without prejudice to any other actions that SEBI may take in accordance with securities laws.

-Sd-

DATE: October 05, 2018

PLACE: Mumbai

MADHABI PURI BUCH

WHOLE TIME MEMBER

SECURITIES AND EXCHANGE BOARD OF INDIA