GAHC010083382018

# THE GAUHATI HIGH COURT
## (HIGH COURT OF ASSAM, NAGALAND, MIZORAM AND ARUNACHAL PRADESH)

**Case No. : WP(C) 2572/2018**

1:ASSAM COMPANY INDIA LTD. AND ANR.
A COMPANY INCORPORATED UNDER THE PROVISIONS OF THE COMPANIES ACT,1956 AND HAVING ITS REGISTERED OFFICE AT GREEN WOOD TEA ESTATE, P.O. DIBRUGARH, ASSAM, REP. BY ITS MANAGING DIRECTOR ADITYA KUMAR JAJODIA, S/O LT. KRISHNA KUMAR JAJODIA, AGED 55 YEARS, PRESENTLY RESIDING AT 3 BHAGWAN DAS ROAD, NEW DELHI- 110001

2: ADITYA KUMAR JAJODIA
PRESENTLY RESIDING AT 3 BHAGWAN DAS ROAD
NEW DELHI-110001

VERSUS

1:THE UNION OF INDIA AND 2 ORS.
REP. BY THE SECRETARY TO THE GOVT. OF INDIA, MINISTRY OF CORPORATE AFFAIRS, GOVT. OF INDIA, 5TH FLOOR, A -WING, SHASTRI BHAVAN, DR RAJENDR APRASAD ROAD,
NEW DELHI- 110001.

2:THE SECURITIES AND EXCHANGE BOARD OF INDIA
A BODY FORMED AND CONSTITUTED UNDER THE CONSTITUTED UNDER THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT AND HAVING ITS OFFICE AT SEBI BHAVAN
PLOT NO. C4-A
'G' BLOCK
BANDRA KURLA COMPLEX
BANDRA (E)
MUMBAI- 400051
REP. BY ITS CHAIRMAN.

3:THE UNION OF INDIA
THROUGH THE DIRECTOR OF INVESTIGATION
HAVING ITS OFFICE AT AAYKAR BHAVAN

P-13
CHOWRINGHEE SQUARE
KOLKATA- 700069

**Advocate for the Petitioner** : MR. D CHOUDHURY

**Advocate for the Respondent** : MR. S C KEYAL(ASSTT.S.G.I.)

**BEFORE**
**HONOURABLE MR. JUSTICE UJJAL BHUYAN**

**ORDER**

**Date : 07-03-2019**

Heard Mr. Ajay Gaggar, learned counsel for the petitioners; Mr. S.C. Keyal, learned Assistant Solicitor General of India for respondent Nos.1 and 3; and Ms. M. Hazarika, learned Senior counsel assisted by Ms. S. Khound, learned counsel for respondent No.2.

**2**. By filing this petition under Article 226 of the Constitution of India, petitioners seek quashing of Annexure-G letter dated 09.06.2017 in respect of petitioner No.1 at Serial No.2.

**3**. Petitioner No.1 is Assam Company Ltd represented by its Managing Director Shri Aditya Kumar Jajodia, petitioner No.2.

**4**. Petitioner No.1 is a company incorporated under the provisions of the *Companies Act, 1956* having its registered office at Greenwood Tea Estate, Dibrugarh.

**4.1**. Petitioner No.1 is involved in the business of cultivation and manufacture of tea having several tea estates in the State of Assam. As per Annexure-B statement annexed to the writ petition, petitioner No.1 has 14 tea estates in the State of Assam producing approximately 11 million kgs of tea per year which are sold either through auction or through private sale. Petitioners have also annexed balance-sheet of

petitioner No.1 for the last five years including annual report for the year 2016-2017. Petitioner No.1 is an income tax assessee and has been submitting income tax returns regularly. Income tax return submitted for the assessment year 2017-2018 has been annexed to the writ petition as Annexure-F. It is stated that besides income tax, petitioner No.1 has been regularly paying other statutory dues and taxes. In addition to tea, petitioner No.1 has extended its business operation to oil exploration.

**4.2**. It is stated that on 07.08.2017, petitioners came to learn that respondent No.2, i.e., Securities and Exchange Board of India (SEBI) had initiated proceedings against petitioner No.1 by instructing Bombay Stock Exchange, National Stock Exchange and Metropolitan Stock Exchange to restrict and/or to suspend trading of shares of petitioner No.1. Petitioners further came to learn that respondent No.2 had initiated such proceedings on the basis of a letter dated 09.06.2017 received from Government of India in the Ministry of Corporate Affairs forwarding the database of 331 listed *shell companies* for initiating necessary action. In the said list of 331 *shell companies*, petitioner No.1 was listed at Serial No.2 with the source indicated as income tax department.

**4.3**. Petitioner No.1 represented before respondent No.2 on 08.08.2017 contending that it is a running company and could not be included in the list of *shell companies*. It was pointed out that petitioner No.1 produces 11 million kgs of tea and employs about 20 thousand workers across the tea estates.

**4.4**. According to the petitioners, no steps were taken by respondent No.2 on the representation of petitioner No.1. Therefore, petitioner No.1 was compelled to file appeal before the Securities Appellate Tribunal, Mumbai which was registered as Appeal No.196/2017. The appeal was disposed of vide order dated 21.08.2017 by directing the stock exchanges to reverse their decision expeditiously while granting liberty to petitioner No.1 to make a representation to respondent No.2 against the letter dated 07.08.2017 which was directed to be disposed of in accordance with law. It was further observed that the aforesaid order would not come in the way of respondent No.2 as well as the stock exchanges from investigating the case of petitioner No.1 and to initiate proceedings if deemed fit.

**4.5**. In compliance to such order of the Appellate Tribunal, petitioner No.1 submitted several representations before respondent No.2 and also sought for copies of documents on the basis of which respondent No.2 had declared petitioner No.1 as a *shell company* which were handed over to petitioner No.1 on 25.01.2018.

**4.6**. According to the petitioners, from the documents handed over to them, it was found that the aforesaid letter dated 09.06.2017 had forwarded a compact disc (CD) received from the Serious Fraud Investigation Office of Government of India, Ministry of Corporate Affairs (SFIO) which included the database of 124 listed companies which were received from the income tax department having been identified in various search/seizures.

**4.7**. From the database, it appears that petitioner No.1 was shown as a company controlled by one Shri Vijay Kumar Gupta who is an entry operator and against whom several income tax proceedings are pending. A nexus was drawn between Shri Vijay Kumar Gupta and petitioner No.1 through Shri Sanjay Khandelwal who is one of the independent Directors of petitioner No.1 and also a Director in the companies controlled by Shri Vijay Kumar Gupta.

**4.8**. Petitioners have vehemently denied that petitioner No.1 has any link with Shri Vijay Kumar Gupta. Mere presence of Shri Sanjay Khandelwal as an independent Director of petitioner No.1 who is also a Director in the companies controlled by Shri Vijay Kumar Gupta cannot be construed as there being a nexus between petitioner No.1 and Shri Vijay Kumar Gupta.

**4.9**. In the meanwhile, respondent No.2 passed an interim order dated 08.12.2017. By the said order trading in securities of petitioner No.1 was reverted to the status as it stood prior to issuance of the letter dated 07.08.2017. It was ordered that stock exchanges would appoint independent auditors to verify misrepresentation of finance and business of petitioner No.1 as well as misuse of funds/books of accounts of petitioner No.1. Promoters and directors of petitioner No.1 were permitted only to buy securities of petitioner No.1, prohibiting them from transferring shares held by them.

**4.10**. Petitioners have contended that passing of such order by respondent No.2 was

not justified. Petitioner No.1 cannot be treated as a *shell company*. Shri Vijay Kumar Gupta had filed affidavit before respondent No.2 stating that he had no association with petitioner No.1 in any manner. Income tax department had not initiated any proceeding against petitioner No.1.

**5**. Being so aggrieved, present writ petition has been filed seeking the relief as indicated above.

**6**. This Court by order dated 18.05.2018 had issued notice both on the writ petition as well as on the interim prayer.

**7.** Respondent No.1 has filed affidavit through Dr. Ramesh Kumar, Registrar of Companies, Shillong. It is stated that petitioner No.1 was incorporated under the *Companies Act, 1956* on 15.03.1977 having its registered office at Greenwood Tea Estate, Dibrugarh in the State of Assam. Objective of the company is to deal in the business of manufacture, export, import, etc in tea, coffee, cinchona, rubber, cocoa and other produces of the soil and to carry on and engage in the business of cultivation of vegetables, extraction of mineral or other produces of the soil and to sell them either through wholesale or in retail. The authorized capital of petitioner No.1 is 60 crores divided into 60 lakhs shares of Rs.10 each and its paid-up capital is Rs.30,97,60,963.00. Petitioner No.1 filed last balance sheet on 31.03.2017 with corresponding annual return up-to 31.03.2017.

**7.1.** Petitioner No.1 is a listed company. Respondent No.1 forwarded a letter dated

23.05.2017 received from SFIO to respondent No.2, SEBI through letter dated 09.06.2017 for necessary action only to safeguard public interest. The said letter was issued by respondent No.1 on the basis of SFIO letter dated 23.05.2017 enclosing a list of 331 companies including the names of companies received from the income tax department which were identified as *shell companies* during various search/seizures. It is stated that petitioner No.1 was identified by SFIO as one out of the 331 companies listed as *shell companies* and its source is the income tax department. Securities Appellate Tribunal had already passed order dated 21.08.2017 on the appeal filed by the petitioners staying the order of respondent No.2 suspending trading of shares of petitioner No.1 in the stock exchanges. Respondent No.2 passed an order dated 08.12.2017 directing the stock exchanges to appoint forensic auditors to verify misrepresentation and misuse of funds, etc of petitioner No.1.

**7.2.** It is contended that respondent No.1 has not committed any illegality in forwarding the information received from an investigating agency, i.e., SFIO to one of the regulators of the capital market, i.e., SEBI for taking action as per law. In such circumstances, respondent No.1 seeks dismissal of the writ petition.

**8.** Respondent No.2, i.e., SEBI in their counter affidavit has stated that it received a letter dated 09.06.2017 from the Ministry of Corporate Affairs, Govt. of India forwarding a copy of letter dated 23.05.2017 of SFIO annexing a list of 331 *shell companies* for initiating necessary action as per SEBI laws and regulations. On receipt

of such letter, respondent No.2 directed the stock exchanges to identify the 331 companies and to place them under stage-IV of credit surveillance measures whereby trading in securities of such companies would stand restricted. In addition, promoters and directors of such companies were only allowed to buy securities in the said listed companies until verification of credentials was completed. Stock exchanges were directed to initiate verification process, if necessary even to conduct forensic audit. Upon such verification, if the stock exchanges do not find appropriate credentials about existence of the companies, proceedings for delisting should be initiated along with freezing of accounts.

**8.1.** By the subsequent letter dated 09.08.2017, respondent No.2 requested the stock exchanges to seek further documents from such companies, such as, income tax returns, etc. The companies were advised to produce certificates of auditor and the stock exchanges were asked to verify such certificates.

**8.2.** Petitioner No.1 had filed an appeal against such directions before the Securities Appellate Tribunal which vide order dated 21.08.2017 had stayed the directions of respondent No.2 restricting trading in securities and buying of securities by promoters and directors of petitioner No.1. It is stated that with effect from 21.08.2017, trading in the securities of petitioner No.1 was reverted to the status as it stood prior to issuance of letter dated 07.08.2017. Besides, such restrictions imposed on promoters and directors of petitioner No.1 were discontinued.

**8.3.** It is stated that respondent No.2 received representation from petitioner No.1 on 29.08.2017. After giving opportunity of hearing to the petitioners, respondent No.2 passed an interim order on 08.12.2017. It was ordered that stock exchanges shall appoint independent forensic auditor to verify misrepresentation including finances and/or business of petitioner No.1 and misuse of funds/books of accounts of petitioner No.1. Restrictions were put on promoters and directors of petitioner No.1 by permitting them to buy securities of petitioner No.1 only and not to transfer their shares in petitioner No.1 by way of sale.

**8.4.** It is further stated that National Company Law Tribunal, Guwahati Bench (Tribunal) vide order dated 26.10.2017 had ordered commencement of corporate insolvency resolution process against petitioner No.1 appointing Shri Vinod Kumar Kothari as the interim resolution professional to carry out functions under the *Insolvency and Bankruptcy Code, 2016*. Thereafter by order dated 12.01.2018, Tribunal appointed resolution professional to conduct corporate resolution process.

**8.5.** Respondent No.2 has stated that petitioner No.1 has not filed its submissions in terms of the interim order dated 08.12.2017 giving liberty to petitioner No.1 to file objection to the aforesaid order.

**8.6.** Contention of respondent No.2 is that petitioner No.1 being under the corporate insolvency resolution process and resolution professional having been appointed by the Tribunal, petitioner No.2 has no *locus* or authority to represent

petitioner No.1 and to file the writ petition. Management of the affairs of petitioner No.1 having been vested with the resolution professional, petitioner No.2 cannot act for and on behalf of respondent No.1. Therefore, at the instance of petitioner No.2, writ petition is not maintainable.

**8.7.** Finally, it is contended that respondent No.2 has acted in accordance with law by rightly directing the stock exchanges to initiate forensic audit in order to reach a definite and conclusive finding. Therefore, respondent No.2 seeks dismissal of the writ petition.

**9.** Petitioners have filed rejoinder affidavit to the affidavit filed by respondent No.2 and has also filed an additional affidavit to place on record certain documents and orders.

**10.** Mr. Gaggar, learned counsel for the petitioners, submits that decision of the respondents to treat petitioner No.1 as a *shell company* on the basis of certain inputs from the income tax department as would be evident from the letter dated 09.06.2017 of the Govt. of India, Ministry of Corporate Affairs to respondent No.2, SEBI is not at all justified inasmuch as a company like petitioner No.1 cannot be termed as a *shell company* under any circumstances. Referring to the interim order passed by this Court on 12.07.2018, he submits that the expression *shell company* has a definite criminal connotation having far reaching consequences. An established company cannot simply be branded as a *shell company* and thereafter subjected to enquiry and

investigation by SEBI to justify such branding. This Court had rightly taken the view that prior notice and hearing ought to have been given to petitioner No.1 before recording of such finding. Therefore, interim order was rightly passed by this Court which should be confirmed.

**11.** On the other hand, Mr. S.C. Keyal, learned Assistant Solicitor General of India submits that SFIO had collated the data of 331 listed *shell companies* obtained from various sources and thereafter forwarded the same to SEBI for initiating action as per law. So far petitioner No.1 is concerned, information was received from income tax department whereafter petitioner No.1 was so identified. SFIO had only forwarded the case of petitioner No.1 to SEBI for investigation. Interference by the Court at this stage may not be justified.

**12.** Ms. M. Hazarika, learned Senior counsel appearing for respondent No.2, SEBI at the outset argued on the point of maintainability of the writ petition at the instance of petitioner No.2. She submits that National Company Law Tribunal, Guwahati Bench vide order dated 26.10.2017 had ordered commencement of corporate insolvency resolution process under the *Insolvency and Bankruptcy Code, 2016* (Code) in respect of petitioner No.1 whereafter an interim resolution professional was appointed to carry out the functions under the aforesaid Code. By subsequent order dated 12.01.2018, National Company Law Tribunal, Guwahati Bench appointed resolution professional to conduct corporate resolution process. Referring to various provisions

of the Code, she submits that upon commencement of corporate insolvency resolution process, Board of Directors of petitioner No.1 has become non-functional; management of petitioner No.1 being vested first with the interim resolution professional and thereafter with the resolution professional. In such a situation, resolution of the Board of Directors of petitioner No.1 authorising petitioner No.2 to initiate legal action on behalf of petitioner No.1 would have no legal sanctity. The resolution professional cannot also ratify such resolution of the Board of Directors. Petitioner No.2 is not competent to file writ petition on behalf of petitioner No.1. Therefore, writ petition so filed would not be maintainable. Resolution of the Board of Directors being illegal, question of ratifying such an illegal act by the resolution professional does not arise inasmuch as such ratification would be *non est* in the eye of law. Further submission of Ms. Hazarika is that resolution plan of petitioner No.1 having been approved, present petitioners cannot pursue the writ petition.

**12.1.** On merits, Ms. Hazarika submits that after receipt of the impugned letter dated 09.06.2017, SEBI took preemptive interim measures in accordance with Section 11(1) of the *Securities and Exchange Board of India Act, 1992* (SEBI Act) in the interest of the investors. Such action is within the purview of law. Petitioner No.1 had availed appellate remedy under the Act by filing appeal before the Securities Appellate Tribunal. While disposing of the appeal, Appellate Tribunal granted liberty to petitioner No.1 to submit representation before SEBI clarifying that order of the Appellate Tribunal would not come in the way of SEBI as well as stock exchanges to

investigate the case of petitioner No.1 and to initiate proceedings, if deemed fit. Thereafter, petitioner No.1 submitted representation before SEBI and an opportunity of personal hearing was granted by SEBI to the authorized representative of petitioner No.1 who made submissions. After considering the information furnished by petitioner No.1, SEBI passed the interim order dated 08.12.2017 against which no appeal has been preferred by the petitioners. Even after passing of the interim order, SEBI permitted inspection of documents by petitioner No.1. However, thereafter petitioner No.1 has not appeared before SEBI; rather request was made to defer the hearing till disposal of the present writ petition. Interim order of SEBI dated 08.12.2017 has not been assailed by the petitioner.

**12.2.** Ms. Hazarika, learned Senior counsel for respondent No.2 submits that it is the duty of SEBI to investigate and make enquiry with regard to any company when some irregularities are brought to its notice. This is done to protect the interest of investors and to regulate the securities market. In support of her submissions, learned Senior counsel has placed reliance on the following decisions:-

1. ***(1989) 3 SCC 132 = Marathwada University Vs. Seshrao Balwant Rao Chavan*** (in support of her contention that there cannot be ratification of an irregularity);

2. ***(2012) 1 SCC 314 = Bar Council of Maharashtra and Goa Vs. Manubhai Paragji Vashi*** (in support of the contention that ratification of an illegality will not validate the illegality).

3. ***(2010) 3 SCC 764 = Securities and Exchange Board of India Vs. Ajay Agarwal*** (in support of the contention that Securities and Exchange Board of India Act, 1992 is a social welfare legislation seeking to protect the interest of small investors. Therefore, it becomes the duty of the Court to adopt an interpretation which furthers the purpose of law rather than that which frustrates it. Besides power to issue directions under Section 11B thereof being procedural in nature can be applied retrospectively).

4. ***(2018) 1 SCC 407 = Innoventive Industries Ltd Vs. ICICI Bank*** (in support of the contention that a legal action at the instance of erstwhile director of the company when *Insolvency and Bankruptcy Code, 2016* has come into play would not be maintainable).

**13.** In his reply submissions, Mr. Gaggar has contended that notwithstanding initiation of proceedings against petitioner No.1 under the Code, Board of Directors of the company does not loose *locus* to institute a legal action. This would be evident from the various orders passed by the Tribunal in the case of petitioner No.1. His submission is that though Board of Directors stands suspended, all the directors and employees of the company are required to assist the resolution professional in managing the affairs of the company during the period of moratorium. That is why resolution professional has ratified the resolution of the Board of Directors to authorize petitioner No.2 to institute legal proceedings. Therefore, petitioner No.2 has the standing to institute the present writ petition along with petitioner No.1.

**14.** Submissions made by learned counsel for the parties have been carefully considered.

**15.** Since the entire *lis* centers around declaration of petitioner No.1 as a *shell company* and thereafter initiating proceeding against petitioner No.1 as a *shell company*, it would be apposite to discuss what is a *shell company* or its legal connotation at the outset.

**16.** The expression *shell company* has not been defined under any law in India. Therefore, there is no statutory definition of *shell company*, be it in fiscal statutes or in penal statues. Neither the *Companies Act, 1956* nor the *Companies Act, 2013* defines the expression *shell company*. In the interim order passed on 12.07.2018, this Court observed that in the Concise Oxford English Dictionary, 11th Revised Edition, *shell company* has been defined as a non-trading company used as a vehicle for various financial manoeuvres.

**16.1.** In popular parlance, a *shell company* is understood as having only a nominal existence; it exists only on paper without having any office and employee. Just like a shell which has a thick outer covering but is hollow inside, a *shell company* is a corporate entity without having active business operations or significant assets. It may be used as a deliberate financial arrangement providing service as a tool or vehicle of others without itself having any significant assets or operations i.e., acting as a front. Popularly *shell companies* are identified as companies which are used for tax evasion or money laundering, i.e., channelizing crime tainted money or proceeds of crime into the formal economy.

**16.2.** But just being a paper company and not having any assets or business operations *per se* is no offence. A corporate entity may be set up in such a fashion with the objective of carrying out corporate activities in future. That would not make it an illegal entity.

**17.** The Organisation for Economic Cooperation and Development (OECD) has prepared a glossary of foreign direct investment terms and definitions. OECD, which was established on December 14, 1960, is now a group of 34 member countries that discuss and develop economic and social policy. OECD members are democratic countries that support free market economies. OECD led a two year effort with G 20 nations to encourage tax reform worldwide and to eliminate tax-avoidance by profitable corporations. In the said glossary, *shell company* has been defined as a company which is formally registered, incorporated or otherwise legally organized in an economy but which does not conduct any operations in that economy other than in a pass-through capacity. Shells tend to be conduits or holding companies and are generally included in the description of special purpose entities.

**17.1.** As per the glossary, special purpose entities have been described as legal entities with little or no employment or operations or physical presence in the jurisdiction in which they are created by their parent enterprises which are typically located in other jurisdictions (economies). They are often used as devices to raise capital or to hold assets and liabilities and usually do not undertake significant

production. An enterprise is usually considered as a special purpose entity if it meets the following criteria:-

(1) The enterprise is a legal entity -

(a) formally registered with a national authority, and

(b) subject to fiscal and other legal obligations of the economy in which it is resident;

(2) The enterprise is ultimately controlled by a non-resident parent, directly or indirectly;

(3) The enterprise has no or few employees, little or no production in the host economy and little or no physical presence;

(4) Almost all the assets and liabilities of the enterprise are the investments in or from other countries;

(5) The core business of the enterprise consists of group financing or holding activities, i.e., chanelling of funds from non-residents to other non-residents.

**18.** Shri Amit Bhaskar, Assistant Professor in Law, Nirma University, Ahmedabad has carried out a study on the subject '*Tackling the Menace of Shell Companies in India*' whereafter he has published an article on the subject. He has stated that there has been a spurt in economic crimes, such as, money laundering, *benami* transaction, tax evasion, generation of black money, round tripping of black money, etc which not only causes revenue and foreign exchange loss to the Government but also creates economic inequality in the society. It may compromise economic sovereignty of the State. According to him, such illegal activities are committed through incorporation of

companies which have neither any asset nor liability nor any operational businesses. These companies exist only on paper to facilitate illegal financial transactions, such as, money laundering and tax evasion. According to him, these kind of companies are called *shell companies*.

**18.1.** In the United States of America, a *shell company* is defined as a registrant with no or nominal operations and either no or nominal assets, assets consisting solely of cash and cash equivalents or assets consisting of any amount of cash and cash equivalents and nominal other assets.

**18.2.** However, it is no offence to be a *shell company per se*. The maximum Registrar of Companies can do is to strike off the name of such company from the register of companies. But if the *shell company* is involved in money laundering or tax evasion or for other illegal purposes, then relevant provisions of laws under the *Prevention of Money Laundering Act, 2002, Prohibition of Benami Transactions Act, 2016, Income Tax Act, 1961* and the *Companies Act, 2013* would be attracted.

**18.3.** As per the study, the necessity for curbing *shell companies* stems from the fact that these companies are incorporated extensively for carrying out illegitimate transactions which aims at money laundering, tax evasion, generation of black money, carrying out *benami* transactions, shifting of corporate profit to tax haven jurisdictions and round tripping of such profit or black money by taking advantage of double tax avoidance treaties thereby causing huge loss in tax revenue. Apprehension has been

expressed by the Financial Action Task Force (FATF) that *shell companies* may be used for financing terrorism. FATF is an inter-governmental policy making body established in the year 1989 to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system.

**18.4.** As per the study, SEBI has proposed to the Government of India that there should be a legal definition of *shell company* as there is no law in India which defines *shell company* at present. Such definition besides giving legal clarity will also enable investigative agencies to carry out investigation more swiftly and in a structured manner.

**18.5.** Parliamentary Standing Committee on Finance has suggested that *shell companies* be defined under the *Companies Act, 2013*. The Committee was of the view that all *shell companies* may not have fraudulent intention. Therefore, the expression *shell company* needs to be defined as having fraudulent intent as one of the characteristic features of such a company.

**19.** Government of India has entered into various treaties with Governments of different countries for avoidance of double taxation and for prevention of fiscal evasion. One such treaty or agreement is the *Indo-Mauritius Double Taxation Avoidance Convention, 1983*. To give effect to such agreement, Central Board of Direct Taxes

(CBDT) issued notification dated 13-04-2000. As per such treaty and the notification, corporate entities incorporated in Mauritius would be liable to taxation only in Mauritius and not in India. Objection was raised to such arrangement on the ground that offshore companies have been incorporated under the laws of Mauritius only as *shell companies* which carry on no business there and are incorporated only with the motive of taking undue advantage of the treaty between India and Mauritius. It was contended that it amounted to unethical and illegal treaty shopping i.e., an act of a resident of a third country taking advantage of a fiscal treaty between two contracting countries. However, in ***Union of India -Vs- Azadi Bachao Andolan, (2004) 10 SCC 1***, Supreme Court repelled such contention and declared the CBDT notification to be valid.

**20.** The question of foreign investments in India being routed through offshore finance centres and also through countries with whom India has entered into treaties came up for consideration in ***Vodafone International Holdings BV –Vs- Union of India, (2012) 6 SCC 613***. In the said decision, Supreme Court turned down the plea for reconsideration of ***Azadi Bachao Andolan*** (supra). Justice Radhakrishnan in his concurring judgment examined the expressions tax haven, treaty shopping, *shell companies* and round tripping. In that context, it was held as under :-

> *" 318. …….. The term "shell companies" finds no definition in the tax laws and the term is used in its pejorative sense, namely, as a company which exists only on paper, but in reality, they are investment companies. ……..."*

**21.** Thus, from the above, what can be deduced is that though a *shell company* is defined in other jurisdictions, in India there is no statutory definition of a *shell company*. However, in popular parlance as well as from the perspective of the Government and its agencies, a *shell company* is ordinarily identified with dubious activities concerning serious economic offences, such as, tax evasion, money laundering, *benami* transaction, conversion of black money into white, round-tripping with host of other associated offences. The general perception is that presence of *shell companies* and its potential use for illegal activities threatens the very economic foundation of the country and severely compromises its economic foundation and ultimately sovereignty.

**22.** Having discussed the above, interim order dated 12.07.2018 passed by this Court may now be adverted to, relevant portion of which is extracted hereunder:-

> "*Petitioner No.1 is a public limited company incorporated under the provisions of the Companies Act, 1956 having its registered office at Dibrugarh and is represented by petitioner No.2, Managing Director. Petitioners are primarily aggrieved by the letter dated 09.06.2017 of the Govt. of India, Ministry of Corporate Affairs addressed to the Chairman, Securities Exchange Board of India (SEBI) forwarding a CD regarding the database of 331 listed shell companies for initiating necessary action by the SEBI.*
>
> *The said letter was issued on the basis of the Office Memorandum (OM) dated 23.05.2017 of the Govt. of India, Ministry of Corporate Affairs, Serious Fraud Investigating Office.*
>
> *From a perusal of the OM dated 23.05.2017, it is seen that a meeting was held on 23.05.2017 at 1100 hrs in the conference room of the Secretary, Ministry of Corporate Affairs regarding discussion on sharing of database of listed shell companies with*

*SEBI. The database comprises of 331 companies out of which 124 companies were earmarked on the basis of information received from the Income Tax department following search and seizure. At Serial No.2 in the list of 331 such companies is the petitioner No.1 company.*

*This Court by order dated 18.05.2018 had issued notice both on the writ petition as well as on the interim prayer. Relevant portion of the order dated 18.05.2018 reads as under:-*

*"By this writ petition, the petitioners challenge the notice dated 9.6.2017 whereby necessary action was directed to be taken by the Chairman, Security Exchange Board of India (SEBI), in respect of 331 listed shell companies as per SEBI laws and regulations. In the said list, name of the petitioners appears at serial No. 2.*
*This petition was filed on 24.4.2018 challenging the aforesaid notice.*
*It is submitted by Mr. Choudhury that based on the said notice, the daily trading in the securities of the petitioner company in the Stock Exchange was suspended against which the petitioner preferred an appeal being Appeal No. 196 of 2017 before the Security Appellate Tribunal, Mumbai and an interim stay was granted and the petitioners were allowed to continue in trading. He also prays for an interim order in terms of the prayer made in the petition.*
*Mr. Keyal submits that he would like to file an affidavit.*
*Issue notice of motion, returnable on 22.6.2018*
*No formal steps are called for with regard to respondent Nos. 1 and 3 as they are duly represented. However, extra copies be served.*
*Steps on respondent No. 2 by registered post with A/D.*
*I ssue notice also on the interim prayer, returnable on 22.6.2018."*

*Mr. Saha, learned Senior counsel, submits that there is no statutory definition of shell company in either fiscal or in the penal statutes. There is also no judicially evolved definition of shell companies. He submits that as per the definition given in Concise Oxford English Dictionary, 11th (Revised) Edition, shell company has been defined as a non-trading company used as a vehicle for various financial manoeuvres. The submission is that the expression shell company in popular parlance refers to a tainted company which is used as a front for routing of crime tainted money into the economy. Therefore, the expression itself has an adverse consequence, penal as well as financial. Before terming the petitioner company No.1 as a shell company, notice ought to have been issued and a hearing ought to have been afforded because*

*terming the petitioner No.1 as a shell company by itself would carry adverse consequences.*

*On the other hand, Mr. Keyal, learned Assistant Solicitor General of India, submits that proceedings against the 331 shell companies have been initiated by the SEBI and an interim order was passed on 08.12.2017 in the case of the petitioner No.1 company wherein adverse observations have been made regarding genuineness of investments made by the petitioner No.1 company and regarding financial misrepresentation. SEBI has also observed that the short-term and long term loans and contractual relationship with companies associated with petitioner No.1 company gives rise to suspicion regarding the genuineness and bona fides of the transactions. SEBI has directed independent forensic audit and issued certain interim directions like giving opportunity to petitioner No.1 company to submit their response. He, therefore, submits that no interim order may be passed as any such interim order may adversely impact the proceedings before the SEBI.*

*Supporting the submissions made by Mr. Keyal, Ms. Hazarika, learned Senior counsel, submits that proceedings before the SEBI may be permitted to continue where petitioners would get adequate opportunity to defend themselves.*

*Submissions made by learned counsel for the parties have been considered.*

*As would be evident from the order dated 08.05.2018, today is fixed for consideration of the interim prayer.*

*In this connection, let us advert back to the impugned letter dated 09.06.2017.*

*Prima facie, this letter declares petitioner No.1 company to be a shell company. This declaration of petitioner No.1 as a shell company as discussed above would entail adverse consequences upon the petitioners. We have already discussed the expression shell company as is understood in popular parlance. Therefore, before declaring a company to be a shell company, it was necessary on the part of the Ministry of Corporate Affairs to have at least put the company on notice that it was being branded as a shell company but that was not done in the instant case.*

*Learned counsel for the petitioners has referred to the averments made in the writ*

*petition and submitted that petitioner No.1 company is an old and reputed company owning 14 Tea Estates in the State of Assam producing 11 million kgs of tea every year. It has a labour force of 20 thousand of its own. Prima facie, branding a company like the petitioner No.1 company as a shell company and thereafter initiating proceeding to prove the same virtually amounts to giving a finding first and thereafter initiating proceeding to justify the finding, like a post decisional hearing. Court is, therefore, of the view that an interim order is called for in this case.*

*Accordingly, impugned letter dated 09.06.2017 in respect of petitioner No.1 company shall remain stayed."*

**23.** Thus, while passing the interim order as extracted above, this Court took the *prima facie* view that since declaration of petitioner No.1 as a *shell company* by itself would entail adverse consequences, petitioner No.1 should have at least been put on notice before being branded as a *shell company*. It was recorded that petitioner No.1 is an old and reputed company owning 14 tea estates in the State of Assam producing 11 million kgs of tea every year and having a labour force of 20 thousand of its own. Therefore, branding such a company as a *shell company* was not justified. Besides, initiating proceedings after branding petitioner No.1 as a *shell company* virtually amounted to giving a finding first and thereafter initiating a proceeding to justify the finding like a post-decisional hearing. One cannot be declared guilty first and thereafter subjected to a trial to justify or uphold such finding of guilt. The letter dated 09.06.2017 and the office memorandum dated 23.05.2017 are very clear. Those clearly proceed on the basis that petitioner No.1 is a *shell company* and not a suspected *shell company*.

**24.** In the appellate order dated 21.08.2017, Securities Appellate Tribunal considered the annual turnover of petitioner No.1 for the last three years which even according to SEBI *prima facie* appeared to be correct and stayed the restrictions imposed by SEBI in trading of shares of petitioner No.1 in the stock exchanges.

**25.** SEBI in its interim order dated 08.12.2017 passed under various provisions of SEBI Act recorded that there were significant governance issues in respect of petitioner No.1 leading to suspicion of misuse of funds by petitioner No.1 including genuineness of investment and financial dealings. Suspicion has been raised against certain transactions. *Prima facie* observations have been made against misuse of books of accounts/funds of petitioner No.1.

**26.** Registrar of Companies in his affidavit has stated that petitioner No.1 was incorporated as a public limited company under the *Companies Act, 1956* on 15.03.1977 having its registered office at Greenwood Tea Estate, Dibrugarh in the State of Assam. Petitioner No.1 has authorized capital of 60 crores and its paid up capital is Rs.30,97,60,963.00. It had filed its balance-sheet as on 31.03.2017 along with corresponding annual return, besides being an income tax assessee.

**27.** In the face of the above, question for consideration is whether it was justified on the part of the SFIO to brand petitioner No.1 as a *shell company*? Further, was the SEBI justified in investigating petitioner No.1 as a *shell company*?

**28**. In the opinion of the Court, considering the negative implications of being

branded as a *shell company*, it was not justified either on the part of the SFIO or respondent No.2 to treat petitioner No.1 as a *shell company* straightaway and thereafter to initiate investigation to justify such branding. Principles of natural justice would require that before such branding, petitioner No.1 should have been put on notice and afforded a reasonable opportunity of hearing as to why and on what grounds it was being suspected to be a *shell company* and only if the response was found to be not satisfactory, such a finding could have been recorded. A finding of *shell company de hors* any notice or hearing would not be justified having regard to its negative implications and serious consequences. In the case of petitioner No.1, the circumstances and the context in which it has been declared as a *shell company* is a virtual condemnation but it is a condemnation without a hearing. That apart, there is also the question of the State or its agencies using an expression which is not defined in any law.

**29.** Objective of the SEBI Act is to promote orderly and healthy growth of securities market on the one hand and on the other hand to protect the interest of investors. It has power to issue directions if it is satisfied upon enquiry that such direction is necessary in the interest of investors etc. Thus, the power of SEBI to enquire into any infraction of law by corporate entities or to conduct enquiry or to issue direction in exercise of its powers under the SEBI Act is not in dispute. Such a power SEBI undoubtedly has but that is not the question here. The question is whether a person, a juristic person in this case, can be condemned unheard. It goes to the root and is

fundamental that no person can be condemned unheard. Therefore, before branding petitioner No.1 as a *shell company*, it was obligatory on the part of respondent No.1 to have issued notice and to have heard petitioner No.1.

**30.** That having not been done, declaration or branding of petitioner No.1 as a *shell company* cannot be legally sustained.

**31.** In so far maintainability of the writ petition at the instance of petitioner No.2 is concerned, Court is of the view that it is the company which is staring at being branded as a *shell company* with all its negative connotations; rather it has already been branded as a *shell company*. The interim resolution professional or resolution professional under the Code has a definite role to play as per the said Code. Its involvement is limited to that extent. Under the Code where any corporate debtor commits a default, a financial creditor, an operational creditor or the corporate debtor itself may initiate corporate insolvency resolution process in respect of such corporate debtor. The corporate insolvency resolution process shall commence from the date of admission of the application filed in this regard. The adjudicating authority shall appoint an interim resolution professional and thereafter the resolution professional whose mandate is to conduct the entire corporate insolvency resolution process and manage the operation of the corporate debtor during the corporate insolvency resolution process period. But it is the directors of the company or persons who were at the helm of affairs of the company at the relevant time who would be directly

affected by declaration of the company as a *shell company* as it is they who would have to face the consequences of such declaration. Therefore, to say that such persons do not have the *locus standi* to assail a finding of being branded as a *shell company* would be wholly untenable. As a matter of fact, Securities Appellate Tribunal entertained the appeal of petitioner No.1 so also SEBI entertained the representation of the petitioners. If they can file appeal before the Securities Appellate Tribunal and file representation before SEBI, it would be wholly illogical to take the stand that they would have no *locus standi* to challenge branding of petitioner No.1 as a *shell company*. It is in the above context that authorisation of petitioner No.2 to initiate legal action on behalf of petitioner No.1 has to be seen. The delegation of authority to petitioner No.2 has been placed on record as Annexure-A to the counter filed by the petitioners to the application filed by respondent No.2 SEBI for vacating the interim order dated 12-07-2018 which was registered as IA (C) No. 2932 of 2018. This delegation of authority was signed by the resolution professional for petitioner No.1 on 23-04-2018. Be it stated that IA (C) No.2932/2018 was dismissed vide order dated 13-09-2018.

**32.** The decisions cited at the Bar and relied upon by learned counsel for respondent No.2 are clearly distinguishable on facts and would not be attracted in the present case. In ***Innovative Industries Ltd.*** (supra), application filed by the financial creditor for initiating corporate insolvency resolution process was admitted by the National Company Law Tribunal and a moratorium was declared. Against such decision appeal was filed by the corporate debtor before the Appellate Tribunal which

was however dismissed. It was in that context that Supreme Court held that appeal at the behest of the erstwhile directors of the appellant (corporate debtor) was not maintainable. The same is not the case here. Challenge is not to the corporate insolvency resolution process but to the branding of petitioner No.1 as a *shell company* the consequences of which will be directly on the petitioners.

**33.** Therefore, upon thorough consideration of the matter, writ petition is not only maintainable but deserves to be allowed.

**34.** Impugned letter dated 09.06.2017 in respect of petitioner No.1 is accordingly interfered with and is set aside.

**35.** Writ petition is allowed but without any order as to costs.

**JUDGE**

**Comparing Assistant**