BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No. 74 of 2007

Date of decision : 5.6.2008

1. Nirma Industries Limited
2. Nirma Chemical Works Limited ….. Appellants

Versus

Securities and Exchange Board of India ….. Respondent

Mr. Janak Dwarkadas Senior Advocate with Mr. Somashekhar Sundaresan, Mr. Karan Bharihoke, Mr. Ankit Lohia and Mr. Zerick Dastoor Advocates and Mr. Hitesh Buch, Practicing Company Secretary for Appellants.

Dr. Mrs. Poornima Advani Advocate with Ms. Sejal Shah Advocate for the Respondent.

Coram : Justice N.K. Sodhi, Presiding Officer

Arun Bhargava, Member

Utpal Bhattacharya, Member

Per : Justice N.K. Sodhi, Presiding Officer

Challenge in this appeal is to the communication dated April 30, 2007 sent by the Securities and Exchange Board of India (hereinafter called the Board) to LKP Shares and Securities Limited, Mumbai – the merchant banker of the appellants informing it that the request for withdrawal of the open offer made on behalf of the appellants is not accepted. The undisputed facts giving rise to this appeal lie in a narrow compass and these may first be noticed.

2. Shree Rama Polysynth Pvt. Ltd., East-West Polyart Ltd. and Ideal Petroproducts Ltd., are group companies of Shree Rama Multitech Limited – a public limited company incorporated under the provisions of the Companies Act, 1956 and hereinafter referred to as the target company. These three companies issued secured optionally fully convertible premium notes for an issue price of Rs.1 lac each having nominal value of Rs.1.35 lacs each to the appellants herein namely, Nirma Industries Limited, Ahmedabad and Nirma Chemical Works Limited Ahmedabad, which are also group companies. These premium notes were issued by way of subscription agreements and a total of 4894 premium notes had been issued to the appellants. The issuer companies agreed to pledge equity shares of the target company in favour of the appellants in order to secure the redemption of the premium notes. The agreements were executed on March 22, 2002 and a total of 1,42,88,700 shares of the target company were pledged with the appellants. The pledge was recorded in the records of the respective depositories in accordance with law. The subscription agreements contained the customary enforcement provisions that entitled the appellants to accelerate payment on the premium notes and to invoke the pledge upon the occurrence of any default. In terms of the enforcement provisions, the appellants by their respective notices dated June 10, 2005 called upon each of the issuer companies to redeem the outstanding premium notes within a period of 30 days from the date of the notice, failing which the appellants would be constrained to invoke the pledge. Since the premium notes were not redeemed within the time specified in the notice, the pledge was invoked by the appellants on July 22, 2005 and the pledged shares were acquired. As the pledged shares constituted 24.25 per cent of the target company's total paid up equity capital, the provisions of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (for short the takeover code) were triggered and Regulation 10 thereof became applicable. This Regulation requires that no acquirer shall acquire shares which entitle him to exercise 15 per cent or more of the voting rights in a company unless he makes a public announcement to acquire shares of that company in accordance with the takeover code. Since the provisions of the takeover code were attracted, the appellants immediately appointed a merchant banker, created the required escrow account and authorized the merchant banker to make a public announcement. The merchant banker made the public announcement on July 26, 2005 to enable the appellants to acquire further shares of the target company. The draft letter of offer was filed with the Board on August 8, 2005 in terms of Regulation 18(1) of the takeover code. The Board issued its letter of observations on April 26, 2006. Soon thereafter, the appellants addressed a detailed letter dated May 4, 2006 to the Board requesting it to exempt the acquirers (appellants) from the operation of Regulation 10 of the takeover code or to permit them to withdraw the public announcement issued on July 26, 2005. In the alternative, the appellants requested the Board to allow them to re-fix the offer price on the basis of the market price of the shares of the target company then prevalent on the date of the letter. A copy of this letter was endorsed to the merchant banker as well. It appears that the merchant banker had discussions with the officers of the Board and informed the appellants that the Board does not take cognizance of such requests made by the acquirers and that such a request shall have to be made through the merchant banker. The merchant banker as per letter dated June 27, 2006 informed the appellants as under:

> "We have perused the various grounds you have mentioned in your above letter to SEBI and are unable to find any of these as valid grounds in terms of the provisions of Regulation 27 of the SEBI (Substantial Acquisition of Shares & Takeovers) Regulations, 1997. The fact that the market price of the target company is far below the offer price

cannot be a reason for seeking withdrawal of the offer. Regulation 27(1) of the Takeover code is the only regulation permitting withdrawal of public offers and the same is reproduced below:
……………………………….”

It appears that after some correspondence between the appellants and the merchant banker, the latter addressed a detailed communication dated September 22, 2006 to the Board with a request to allow the appellants to withdraw the offer. Special circumstances, which according to the merchant banker, came to the notice of the appellants much after the public announcement were mentioned in the communication on the basis of which the withdrawal of the offer was sought. It is pertinent to mention that the special circumstances mentioned by the merchant banker were the same which the appellants had mentioned in their letter of May 4, 2006. The request made by the merchant banker on behalf of the appellants was considered by the deputy general manager exercising the delegated authority of the Board and by her order dated April 30, 2007 the request to withdraw the public offer was declined. It was pointed out that the appellants should have done their due diligence before invoking the pledge and should not have acquired the shares if the circumstances so warranted. The special circumstances pointed out by the merchant banker on behalf of the appellants were not, according to the Board, "reasons sufficient enough to merit the withdrawal of the open offer." The Board was of the view that the circumstances mentioned could only mean business misfortune which did not fall in the exceptions mentioned in Regulation 27(1) of the takeover code. Hence this appeal.

3. We have heard Shri Janak Dwarkadas, senior Advocate on behalf of the appellants and Dr. Mrs. Poornima Advocate on behalf of the Board. It was pointed out on behalf of the appellants that the new board of directors of the target company ordered an investigation into its affairs by M/s. Ramesh C. Sharma and Co., Chartered Accountants who filed detailed reports in March 2006 before the High Court of Gujarat in a company petition. These reports referred to some earlier inspection reports pertaining to the year 2002 and all these had shown that a sum of Rs.326.48 crores had been siphoned off by the erstwhile promoters of the target company. It was also urged that these reports came into the public domain only in March 2006 and it was not possible for the appellants despite due diligence to know about the financial affairs of the target company and the conduct of its erstwhile promoters. It was also argued on behalf of the appellants that they could not discover the facts pertaining to the financial health of the target company as they were not even its shareholders. Reference was also made to the report submitted by the Chartered Accountants pointing out that the earlier inspection reports which had highlighted huge contingent liability of the target company had been suppressed from its shareholders and were not disclosed in the balance sheet. It was on this basis that the learned senior counsel sought to argue that when the facts were suppressed from the target company itself, it was not possible for the appellants to unearth those facts. The crux of the arguments on behalf of the appellants is that despite exercise of due diligence it was not possible to discover the facts which were not in the public domain as the appellants could not be expected to play the role of a detective. Reference was also made to some events subsequent to the public announcement which revealed that the target company had lost its substratum and that there was large scale embezzlement in that company. It was contended that the Board ought to have taken note of the aforesaid facts and that it was not justified in observing that there was lack of due diligence on the part of the appellants. According to the learned senior counsel for the appellants the special facts mentioned hereinabove and also in the communications addressed to the Board seeking withdrawal of the public offer were sufficient for it (Board) to allow withdrawal of the

offer. Regulation 27(1) of the takeover code was referred to and it was pointed out that clause (d) thereof which provides for “such circumstances as in the opinion of the board merit withdrawal” gave wide powers to the Board to allow withdrawal particularly when the facts which came to light subsequently were such as could not be discovered by the appellants despite the exercise of due diligence. The learned senior counsel strenuously contended that “such circumstances’ referred to in clause (d) were not to be read ejusdem generis with the preceding clauses. Shri Dwarkadas the learned senior counsel was equally emphatic in contending that the Board while passing the impugned order had violated the principles of natural justice inasmuch as the appellants were not afforded a personal hearing before taking the impugned decision.

4. Dr. Mrs. Poornima Advani seriously controverted the averments made on behalf of the appellants and submitted that the special facts referred to in the communications addressed to the Board seeking withdrawal of the public offer were such as could be discovered after due diligence and that the appellants had failed to carry out their duty before invoking the pledge and acquiring the shares. She strenuously urged that grounds such as financial instability of the target company or additional financial burden on the acquirer as argued on behalf of the appellants are not sufficient to enable the Board to allow withdrawal of the public offer and that the grounds, if accepted, would defeat the very purpose of the takeover code and open floodgates for companies to seek withdrawal of the open offer when they find that they had taken business decisions which subsequently turned out to be bad decisions. She was equally emphatic in contending that the withdrawal of the offer would not be in the interest of investors and the securities market since the acquirer (appellants) would acquire substantial shares/control in the target company without the obligations imposed by the takeover code. Referring to Regulation 27(1) of the takeover code, Dr. Advani strenuously contended that the same should be strictly construed and that the normal rule was that a public offer once made could not be withdrawn. As regards the violation of the principles of natural justice, she submitted that all the contentions raised on behalf of the appellants either by them or by their merchant banker were considered by the Board before the impugned order was passed and they had said in those communications what they wanted to. She further submitted that on the facts of this case it was not necessary to afford a personal hearing to the appellants as such a hearing is not a part of the principles of natural justice.

5. From the rival contentions of the parties, the two questions that arise for our consideration are whether the Board was right in refusing to allow the appellants to withdraw the public offer under Regulation 27(1)(d) of the takeover code and whether this provision is to be construed strictly in the context of the takeover code.

6. Takeover of public listed companies and substantial acquisition of shares in such companies are governed by the takeover code. It is aimed at providing an orderly framework within which the process of substantial acquisition of shares and/or control can be conducted. It provides that if an acquirer acquires more than five per cent shares or voting rights in a company, he has to disclose at every stage the aggregate of his holding to that company and also to the stock exchange(s) where the shares are listed as per the takeover code. Again, if he were to acquire 15 per cent or more of the voting rights, he has to make a public announcement to acquire further shares of that company at a market

related price in terms of the takeover code. In the case of creeping acquisition, the acquirer has to make a public announcement every time he acquires additional shares entitling him to exercise more than five per cent of the voting rights. The takeover code then prescribes the detailed procedure for making the public announcement and the manner in which the offer price is determined at which the shares are offered to public shareholders. Shorn of the other details with which we are not concerned in this case and having regard to the scheme of the takeover code, it is clear that it has a threefold purpose (a) to ensure that the target company is aware of the substantial acquisition, (b) to ensure that in the process of substantial acquisition or takeover, the securities market is not distorted or manipulated, and (c) to ensure that the small investors are given an option to exit, that is, they are offered a choice to either offload their shares at a price as determined in accordance with the takeover code or to continue as shareholders under the new dispensation. In other words, the takeover code is meant to ensure fair and equal treatment of all shareholders in relation to substantial acquisition of shares and takeovers and that the process does not take place in a clandestine manner without protecting the interest of the shareholders. It is in this background that we have to read Regulation 27(1) of the takeover code which is reproduced hereunder for facility of reference:

> " **Withdrawal of offer**.
>
> 27.(1) No public offer, once made, shall be withdrawn except under the following circumstances:-
> (a) (Omitted w.e.f. 9.9.2002)
> (b) the statutory approval(s) required have been refused;
> (c) the sole acquirer, being a natural person, has died;
> (d) such circumstances as in the opinion of the Board merit withdrawal.
>
> (2) ...."

The Regulation starts with the negative words "No public offer, once made, shall be withdrawn except ....which clearly indicate the intention of the framers. They have clothed their command in a negative form which means as a general rule, the public offer once made should not be allowed to be withdrawn. Like most of the rules, this Regulation has also some exceptions which are referred to in clauses (b) to (d). Because they are exceptions, they have to be construed very strictly. This is a well established rule of interpretation. Clause (b) envisages a situation where statutory approval(s) have been refused. It is axiomatic that in such an eventuality it would not be possible for the acquirer to go through or complete the public offer. The law will not permit him to continue with the offer. Death of the sole acquirer who is a natural person is yet another circumstance which may entail the withdrawal of the public offer in terms of clause (c). Here again, death has made it impossible for him to complete the public offer. Then we have clause (d) which refers to "such circumstances as in the opinion of the Board merit withdrawal". This is a residuary clause containing general words. The specific circumstances under which the public offer could be withdrawn are mentioned in clause (b) and (c) followed by the general words in clause (d). In such a situation the rule of ejusdem generis gets attracted and the general words in clause (d) have to be construed as limited to things or circumstances of the same kind as those specified in the preceding clauses. To put it differently, the general words "such circumstances" in clause (d) must draw their colour from the circumstances referred to in clauses (b) and (c). In Amar Chandra vs. Collector of Excise, Tripura AIR 1972 S.C. 1863, the Supreme Court held that the rule of ejusdem generis applies when "(i) the statute contains an enumeration of specific words; (ii) the subjects of enumeration constitute a class or category; (iii) that class or category is not exhausted by the enumeration; (iv) the general terms follow the enumeration;

and (v) there is no indication of a different legislative intent." We are of the considered opinion that all these tests are satisfied in the case before us. We say so because when we read clauses (b) and (c) we find that they refer to circumstances which pertain to a class, category or genus and the common thread that runs through them is the impossibility in carrying out the public offer. "Such circumstances" in clause (d) will have to be read to mean circumstances analogous to those which would make it impossible for the acquirer to go through with the public offer. The framers of the takeover code could not anticipate all such situations which would make it impossible to complete the public offer and, therefore, left it to the Board to decide on a case to case basis whether "such circumstances" exist which may require withdrawal of the offer. It goes without saying that the opinion of the Board in this regard has to be formed on a reasonable basis having regard to the interest of the investors. Far from having a different legislative intent, we are of the view that the object of the takeover code would be better achieved if a restricted meaning, as discussed above, is assigned to the exceptions contained in clauses (b) to (d) of Regulation 27(1). If a liberal meaning is assigned to the words "such circumstances" appearing in clause (d), then not only will the objects of the takeover code get frustrated but the public shareholders will be deprived of their rights thereunder. If an acquirer is allowed to withdraw from the public offer on the asking or even on the ground that he discovered some adverse facts pertaining to the financial health of the target company subsequent to the acquisition/public offer, the interest of the public shareholders will be seriously jeopardised as they will be deprived of their right to exit from the target company which is a valuable right given to them by the takeover code. In A.G. Vs. Brown (1920) 1KB773 the words "any other goods" occurring in section 43 of the Customs (Consolidation) Act 1876 which empowered His Majesty by order in council to prohibit the importation of "arms, ammunition, or gun powder or any other goods" were construed as referring to goods similar to "arms, ammunition or gun powder". In view of our discussion hereinabove, we have no hesitation in holding that "such circumstances" referred to in clause (d) of Regulation 27(1) have to be limited to the kind of circumstances mentioned in the preceding clauses (b) and (c) which would make it impossible for the acquirer to go through with the public offer.

7. We may now deal with the special circumstances pointed out by the appellants and their merchant banker on the basis of which they sought to withdraw from the public offer. It was pointed out that the appellants came to know many months after the public announcement that the target company had lost its substratum. It is stated that the erstwhile directors of the target company who resigned in December 2005 had embezzled large sums of that company which was discovered only after the new board of directors of the target company had got the matter enquired from independent chartered accountants. It is also alleged that the appellants came to know that the Asset Reconstruction Company (India) Ltd. had given notice to the target company under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 to make payment of an amount of Rs.260.32 crores. The notice had been challenged in the High Court of Gujarat in a writ petition which was dismissed and the matter was pending in appeal. This fact also, according to the appellants, came to their notice long after the public announcement. The fact that a petition for winding up of the target company was pending in the High Court which not only stood admitted but had also been advertised, notifying admission of the petition was also relied upon to seek withdrawal from the public offer. Reliance was also placed on some contingent and unrecorded liabilities of the target company and also on the fact that it had been registered as a 'sick company' under the Sick Industrial Companies (Special Provisions) Act, 1985. It was on the basis of these allegations that the appellants wanted to withdraw from the public offer. Having given

our thoughtful consideration to the contentions advanced by the learned senior counsel, we are inclined to agree with Dr. Poornima Advani that there was lack of due diligence on the part of the appellants before invoking the pledge and acquiring the shares of the target company. We are satisfied that the appellants had taken a business decision which might have turned out to be wrong and that they now want to wriggle out of their obligation of a public offer under the takeover code. As already observed, this cannot be allowed as that would deprive the public shareholders of their valuable right to have an exit option under that code. At any rate the circumstances pointed out are not "such circumstances" as referred to in clause (d) of Regulation 27(1) of the takeover code inasmuch as none of them individually or cumulatively make it impossible for the appellants to meet their obligation of carrying out the public offer made under the takeover code.

8. The appellants argued that they were not in a position to exercise due diligence regarding the financial status of the target company since there was no direct nexus between them and the target company. They had merely accepted the shares of the target company on pledge from third parties. It was also their case that even if they could exercise due diligence, they could not possibly unearth any of the financial irregularities in the target company before the public announcement since even the Directors of the target company became aware of these irregularities much later. We have, however, noticed from the record that even at the time of the public announcement, the appellants were in possession of certain facts that clearly showed the poor financial health of the target company. A few instances of such facts are mentioned below:

(i) The fact that Gujarat High Court had admitted a petition by the UTI Bank and Karnataka Bank Ltd. for winding up the target company and that the latter had filed appeals against this order was known to the appellants before making the public announcement.

(ii) The appellants were aware that in September, 2004, the Board had issued directions under section 11B and 11(4) of the Securities and Exchange Board of India Act, 1992 read with Regulation 11 of the FUTP Regulations, 2003 against the target company and its Directors Sree Rama Polysynth Pvt. Ltd. and its Directors and East-West Polyart Ltd. and its Directors, among others, restraining them from accessing the securities market and buying, selling or dealing in securities directly or indirectly for a period of five years in the case of the target company and its Directors and three years for others. The persons so penalized included those whose shares had been pledged with the appellants.

(iii) The fact that the net worth of the target company had been fully eroded by 31.3.2005 was known to the appellants at the time of making the public announcement.

(iv) There were numerous cases pending against the target company and its Directors including cases for recovery of overdue debts and cases regarding bouncing of cheques involving crores of rupees.

The above facts would seem to be enough to provide the appellants a correct prognosis regarding the financial health and prospects of the target company. Clearly, the appellants decided on invoking the pledge on the shares of the target company with open eyes and sufficient knowledge about the affairs of the target company. It is not as if the appellants were innocent and were caught napping in an unexpected turn of events. We are not, therefore, inclined to accept at its face value the argument of the appellants that they had no prior clue about the adverse financial information relating to the target company that were contained in the later reports of the Chartered Accountants. In this view of the matter, the Board was justified in characterising the situation that the appellants are faced with as the result of lack of due diligence and/or sheer business misfortune. They are only trying to wriggle out of a bad bargain which is not permissible under Regulation 27(1)(d) of the takeover code.

9. This brings us to the last contention advanced by the learned senior counsel on behalf of the appellants. It is contended that the Board did not afford any personal hearing to the appellants before taking the final decision on the request made on their behalf for the withdrawal from the public offer and, therefore, the principles of natural justice were flagrantly violated. Here again we are unable to agree with the learned senior counsel. There is no gainsaying the fact that the appellants themselves in their letter dated May 4, 2006 and subsequently their merchant banker in the communication dated September 22, 2006 had stated all the circumstances on which they were relying to seek withdrawal from the public offer and there was nothing more that they had to say. The Board considered all aspects of the matter and declined the request which has been discussed in detail hereinabove. We do not think that it was necessary for the Board to have afforded a personal hearing to the appellants in the circumstances of this case. Having acquired the shares of the target company which breached the threshold limit prescribed by the takeover code, the appellants were required to make a public offer to acquire further shares of that company for which a public announcement was made. The normal rule being that the public offer once made could not be withdrawn, it was only in the exceptional circumstances referred to in the earlier part of our order that such an offer could be withdrawn. The appellants were invoking those exceptional circumstances and the Board having considered the matter took a decision. It is not that they had no opportunity to place their point of view before the Board. In these circumstances, it was not necessary for them to be given a personal hearing. In this view of the matter, it is not necessary for us to deal with the several judgments cited by the learned senior counsel in support of his plea. However, it is necessary to refer to Union of India and another v. Jesus Sales Corporation (1996) 4 SCC 69 wherein the learned judges have clearly held that the principles of natural justice do not require a personal hearing to be granted in every case when a quasi judicial authority has to pass an order on an application filed before it. This is what their Lordships have observed:

> "The courts cannot insist that under all circumstances and under different statutory provisions personal hearings have to be afforded to the persons concerned. If this principle of affording personal hearing is extended whenever statutory authorities are vested with the power to exercise discretion in connection with statutory appeals, it shall lead to chaotic conditions. Many statutory appeals and applications are disposed of by the competent authorities who have been vested with powers to dispose of the same. Such authorities which shall be deemed to be quasi-judicial authorities are expected to apply their judicial mind over the grievances made by the appellants or applicants concerned, but it cannot be held that before dismissing such appeals or applications in all events the quasi-judicial authorities must hear the appellants or the applicants, as the case may be. When principles of natural justice require an opportunity to be heard before an adverse order is passed on any appeal or application, it does not in all circumstances mean a personal hearing. The requirement is complied with by affording an opportunity to the person concerned to present his case before such quasi-judicial authority who is expected to apply his judicial mind to the issues involved. Of course, if in his own discretion if he requires the appellant or the applicant to be heard because of special facts and circumstances of the case, then certainly it is always open to such authority to decide the appeal or the application only after affording a personal hearing."

10. These observations aptly sum up the legal position and apply to the facts before us. We have therefore no hesitation in holding that there was no violation of the principles of natural justice merely because the appellants were not given a personal hearing.

11. No other point was raised.

In the result, the appeal fails and the same stands dismissed leaving the parties to bear their own costs.

Sd/-

Justice N.K. Sodhi

Presiding Officer

Sd/-

Arun Bhargava

Member

Sd/-

Utpal Bhattacharya Member

5.6.2008

ddg/-