MOOT PROBLEM

1. On January 30, 2009, the Promoters of Artemis Limited ("**Artemis**"), a company listed on the Bombay Stock Exchange, borrowed a sum of Rs.100 Crore from Dreamsellers Limited ("**Dreamsellers**") and pledged the equity shares of Artemis Limited as security. A Pledge agreement was entered into in this regard.

2. On June 10, 2010, Dreamsellers, in terms of the enforcement provisions contained in the agreements with the borrower, issued a letter calling upon them to repay the debt within a period of 30 days, failing which Dreamsellers would be constrained to invoke the pledge.

3. The debt was not repaid within the prescribed time. Upon default by the Promoters of Artemis to repay the debt, the pledge was invoked by Dreamsellers on July 22, 2010, which made Dreamsellers entitled to 12.5 per cent equity shares in Artemis.

4. Dreamsellers, even after the invocation of the pledge, was unsure of whether the shares would pay off the debt unless they got a say in the running of Artemis. The Promoters of Artemis were under financial stress and that was bound to have an impact on Artemis too. Thus, it was critical for them, commercially, to see if they could take control over Artemis. The Promoters of Artemis kept promising to Dreamsellers that they were making arrangements to repay, but nothing fructified until September 30, 2010.

5. Therefore, along with the invocation of the pledge, which got them only 12.5 per cent equity shares, Dreamsellers decided to voluntarily make an open offer under Regulation 10 of the Securities and Exchange Board of India (Substantial Acquisition Of Shares And Takeovers), 1997 ("**1997 Takeover Regulations**") to acquire upto 37.6 per cent equity shares in Artemis. If they were to get a full response, their holding would go up to 50.1 per cent of the equity share capital in Artemis.

6. Dreamsellers made a Public Announcement ("**PA**") dated October 1, 2010, published in the Financial Express, Mumbai Edition, for the proposed Open Offer to acquire upto 37.6 per cent equity shares of Artemis. A Draft Letter of Offer was filed with the Securities and Exchange Board of India ("**SEBI**") within the stipulated time of 14 days from the date of the PA. SEBI raised various questions and supplemental questions on various counts and the Draft Letter of Offer was under process in dialogue with the merchant banker of Dreamsellers.

7. Meanwhile, lenders to Artemis had been pushing the Board of Directors to review the operations of Artemis and reminded them of their fiduciary duties. The independent directors who, as non-executive directors would hardly have a day-to-day insight into the company's operations forced the conduct of an internal assurance audit of Artemis' operations and financial statements.

8. Pursuant to the internal audit, certain irregularities in the financials of Artemis Limited between 2005 and 2008 were observed. The Board of Directors of Artemis, under pressure from the independent directors who were part of the Audit Committee, directed a special investigative audit into the financial affairs of the company for the past ten years. An independent chartered accountant firm was appointed to conduct the investigation which proceeded with the inquiry and prepared a report for the board of directors. It was established from the report dated September 30, 2011, that through fraudulent transactions, Rs. 300 crores had been siphoned off and embezzled by the Promoters of Artemis Limited.

9. Thereafter, after deliberations by the board of directors on October 25, 2011, the investigative report was brought into the public domain by the board of directors of Artemis. One of the representatives of the lenders on the board of directors of Artemis filed the report in the legal proceedings that were underway in the Delhi High Court. The public dissemination of the contents of the report resulted in a sharp decline in the prices of shares of Artemis.

10. On October 30, 2011, Dreamsellers wrote through its merchant bankers to SEBI seeking to withdraw the open offer that it had voluntarily made. Dreamsellers' argument was that it had only made an open offer voluntarily and extraordinary facts have since emerged and therefore, it should be permitted to withdraw the open offer. As an alternative and without-prejudice argument, Dreamsellers sought that SEBI should pass an order permitting re-pricing of the open offer price in view of the new facts that have become known, which the market did not know earlier, and because of which the market price had been much higher than what it would have been had the price become known.

11. On November 1, 2011, after a long delay, SEBI issued its "observations" on the Draft Letter of Offer submitted to SEBI. No observations were made regarding the falling price or the embezzlement of funds and SEBI merely stated that the request for withdrawal of the open offer was not being considered favourably. SEBI was silent on the alternative request for re-pricing of the open offer price and merely stated that the offer once made cannot be withdrawn. SEBI stated that acquirers should conduct their due diligence before deciding on whether to make an open offer. Having made it once, they cannot withdraw it lightly, since only circumstances similar to the death of the acquirer or statutory approvals not being provided, could be grounds for withdrawal.

12. Meanwhile, the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ("New Takeover Regulations") had been notified on September 23, 2011 and the same came into force with effect from October 22, 2011.

13. In its observations, SEBI also stated that Regulation 23 of the New Takeover Regulations would not be applicable at all since the open offer had been made under the provisions of the 1997 Takeover Regulations. It was also stated that earlier case law on withdrawal of open offers would be against Dreamsellers.

14. Being aggrieved by the SEBI Order, Dreamsellers filed an appeal before the Securities Appellate Tribunal ("**SAT**") under Section 15T of the SEBI Act, 1992, challenging the same. The grounds of the challenge were:-

a. Dreamsellers had no way of knowing about the state of affairs of Artemis' finances and operations, since the company was a public listed company and only published information was the basis of all its decisions. Fraud vitiates all solemn acts and the discovery of fraud entitles them to withdraw the open offer.
b. The observations issued by SEBI were under the corresponding provisions of the New Takeover Regulations and therefore with the repeal of the 1997 Takeover Regulations, any old case law governing the old regulations would not come in the way at all.
c. The interplay of regulations governing insider trading and takeovers would support its case that there was no question of it being aware of the fraud and had it known of the fraud, it would not have made an open offer.
d. The open offer was not at all triggered by the invocation of the pledge. It was a voluntary open offer and it was not to be treated as SEBI would treat an open offer that is mandatorily triggered by acquisition of 15% or more voting rights in a listed company. Being a voluntary open offer, no one would unfairly lose anything or gain anything if the open offer were permitted to be withdrawn.
e. SEBI had not even dealt with the alternative proposal to re-price the open offer by factoring in the financial impact of the fraud discovered. It had merely stated that the open offer must be made and the acquirer should have checked all facts before venturing out, and that having ventured out, he was bound to proceed with and complete the open offer.
f. SEBI did not conduct any hearing for taking such a vital decision and Dreamsellers was given no opportunity to consider what was weighing with SEBI, and had it known that the grounds and reasoning in SEBI's mind, it would have been able to show cause as to why those reasons were bad in law. Therefore, at the least, the matter ought to be remanded to SEBI so that a ruling on merits could become available.

15. The SAT after hearing the parties passed an order dismissing the appeal filed by Dreamsellers. The SAT, inter alia, held:

a. Regulation 23 of the New Takeover Regulations would not be applicable in the present case as the open offer was made under the provisions of the 1997 Takeover Regulations.
b. Regulation 27 (1) (d) of the 1997 Takeover Regulations is to be given a strict interpretation and the words "*such circumstances as in the opinion of the Board merit withdrawal*" are to be read *ejusdem generis* with the other provisions of Regulation 27 (1) to be limited to only circumstances where it is impossible to make a public offer.
c. The 1997 Takeover Regulations have been well interpreted by the Hon'ble Supreme Court and therefore applying the ratio there, there was no option for the SAT but to uphold SEBI's order.
d. Dreamsellers ought to have conducted proper due diligence before making the open offer. SAT agreed with SEBI's argument that the fact of the large-scale embezzlement in the target company were existent prior to the exercise of the pledge by Dreamsellers and therefore were "known" or "could have been known" by Dreamsellers if Dreamsellers had exercised proper "due diligence".
e. There was no violation of the principles of natural justice in the present case. The correspondence between Dreamsellers and SEBI, and the discussions between Dreamsellers' merchant banker and SEBI addressed all necessary issues and there was no case for a remand.

16. Being aggrieved by the Order of the SAT, Dreamsellers filed an appeal before the Hon'ble Supreme Court under Section 15Z of the SEBI Act, 1992.

17. In its appeal before the Supreme Court it was contended by Dreamsellers that SEBI passed its Order summarily and without seeking explanations and arguments from Dreamsellers on any specific issue that weighed with SEBI. Besides, it was contended that SEBI did not appreciate that fraudulent transactions, systematic embezzlement and siphoning of funds were unearthed by special investigative audit and could not have been found by an outside third party like Dreamsellers before invoking the pledge. The interplay of insider trading regulations and takeover regulations had been missed out completely by both SEBI and the SAT. Any due diligence conducted, could only have been done on published financial information and other information in the public domain, and it would not have become possible for Dreamsellers to know of it.

18. It was also contended that the application for withdrawal was made under Regulation 23 of the New Takeover Regulations after it came into force and after the 1997 Takeover Regulations had been repealed. Earlier decisions on Regulation 27 of the 1997 Takeover Regulations are not applicable at all, and even if so, can be differentiated, and therefore, SEBI and SAT had completely erred in blindly applying old case law on repealed regulations, to this case.

19. Without prejudice to the above and even if Regulation 27 of the 1997 Takeover Regulations was applicable in the present case, it was also contended that the Order of SAT renders a restrictive interpretation to Regulation 27 of the Takeover Regulations, as it restricts the power of SEBI to permit withdrawal only in cases where it is impossible to complete an open offer – in itself a nullity. Therefore, there is a case to be made for constituting a larger bench to reconsider even the earlier rulings of the Supreme Court.

20. SEBI too has filed its reply. The pleadings were complete and the matter was posted for arguments. The Chief Justice of India has constituted a larger bench to look into the matter in detail and if necessary, even reconsider the earlier ratios.

21. The newly constituted bench has framed the following issues:

a. Whether the provisions of Regulation 23 of the New Takeover Regulations relating to withdrawal of open offer could be applied to an open offer made under the 1997 Takeover Regulations?
b. Whether it can be said that Dreamsellers had failed to exercise due diligence and the facts relating to the fraud were "known" or "could have been known" by Dreamsellers, if Dreamsellers had exercised proper "due diligence"?
c. Whether SEBI had violated the principles of natural justice in the present case while passing its order rejecting the application to withdraw the open offer without hearing Dreamsellers?
d. Whether Regulation 27 (1) (d) of the 1997 Takeover Regulations is to be given an interpretation whereby, the words "*such circumstances as in the opinion of the Board merit withdrawal*" are to be read *ejusdem generis* with the other provisions of Regulation 27 (1) of the said code i.e. as circumstances where it is impossible to perform the open offer?

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