BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Date of Decision : 27.06.2020

Misc. Application No. 154 of 2020
(Urgency Application)
And
Misc. Application No. 155 of 2020
(Stay Application)
And
Appeal No. 145 of 2020

Dr. Udayant Malhoutra
A-1/3, Cornwell Road,
Bengaluru,
Karnataka – 560 027. …Appellant

Versus

Securities and Exchange Board of India,
SEBI Bhavan, Plot No. C-4A, G-Block,
Bandra-Kurla Complex, Bandra (East),
Mumbai – 400 051. …Respondent

Mr. Somasekhar Sundaresan, Advocate with Mr. Zerick Dastur, Ms. Smriti Singh, Mr. Khushil Shah and Mr. Kunal Kothary, Advocates i/b Zerick Dastur, Advocates & Solicitors for the Appellant.

Mr. Gaurav Joshi, Senior Advocate with Mr. Abhiraj Arora, Mr. Vivek Shah and Mr. Feroze Patel, Advocates i/b ELP for the Respondent.

CORAM : Justice Tarun Agarwala, Presiding Officer
Dr. C.K.G. Nair, Member
Justice M.T. Joshi, Judicial Member

Per : Justice Tarun Agarwala, Presiding Officer (Oral)

1. The present appeal has been filed against an ex-parte order dated June 15, 2020 passed by the Whole Time Member ('WTM' for short) of Securities and Exchange Board of India ('SEBI' for short) directing the appellant to deposit a sum of Rs. 2,66,59,215/-plus interest till date totaling Rs.3,83,16,230.73 in an Escrow Account towards notional loss allegedly avoided by him by using unpublished price sensitive information and further directed that the bank accounts / demat accounts of the appellant shall remain frozen till such time the amount is not deposited. The WTM further directed the appellant to show cause as to why an order of disgorgement should not be passed.

2. The facts leading to the filing of the present appeal is, that the appellant is the Chief Executive Officer and Managing Director of a listed company known as Dynamatic Technologies Limited ('DTL' for short) which is engaged in the manufacturing of aerospace, automotive and engineered products. The appellant has been the Managing Director since 1989. The charge leveled against the appellant is, that he had sold 51,000 shares of the company DTL on October 24, 2016 having inside knowledge of the price sensitive information, namely, the unaudited financial results of the quarter ending

September 30, 2016. It was alleged that the financial results were approved by the Board of Directors on November 11, 2016 whereupon the price of the scrips of the company drastically went down. It was alleged that the appellant had inside information of the price sensitive information and, being a connected person had sold the shares and thus made a notional gain or averted a notional loss.

3. In this regard, the sales made by the appellant was investigated in 2017 and that the investigation team only asked information from the appellant for the first time on November 28, 2019 and thereafter the WTM passed the impugned exparte order on June 15, 2020.

4. The contention of the appellant is, that there was no urgency in passing an ex-parte order with regard to a trade done by the appellant more than three and half years ago and especially during the pandemic period. It was urged that the action of the respondent in freezing the accounts of the appellant during these time was wholly arbitrary. It was further urged that an ex-parte order cannot be sustained in as much as the same is violative of the principles of natural justice. The appellant contended that the shares were sold on account of a loan agreement entered by the company with a consortium of

banks and that appellant was required to reduce its pledge holdings for the purpose of disbursement of a loan of 3,69,00,00,000 (Rupees Three Hundred and Sixty Nine Crores Only). It was urged that had an opportunity of hearing been given these relevant facts could have been intimated which could have been considered by the respondent. It was also contended that the prices of the scrip went down not because of the disclosure of the financial results of the quarter ending September 30, 2016 but on account of the fact that the Government of India announced the demonetisation of its currency on November 8, 2016 and share prices across the board had declined which factor, being a relevant factor, was not taken into consideration.

5. On the other hand, the respondent contended that an ex-parte interim order cum show cause notice has been issued and if the respondent files a proper reply, the matter could be decided in a short period. It was also contended that the reason for passing an ex-parte interim order was that there may be a possibility of diversion of the notional gain made by the appellant during the pendency of the proceedings. It was also urged that the appellant was an insider and was privy to the unpublished price sensitive information and therefore the WTM

rightly passed the impugned order in order to protect the investors in the securities market.

6. In this regard we have heard Shri Somasekhar Sundaresan, the learned counsel for the appellant and Shri Gaurav Joshi, the learned senior counsel for the respondent.

7. In ***North End Foods Marketing Pvt. Ltd. vs Securities and Exchange Board of India in Appeal No. 80 of 2019 decided on March 12, 2019*** this Tribunal held as under:-

> *"13. Having heard the learned senior counsel at length, we find that it is no more res integra that SEBI has power to pass ex-parte interim orders, pending investigation, which power flows from Section 11 and 11B of the SEBI Act. A plain reading of Section 11 and 11B shows that SEBI has to protect the interests of the investors in securities and to regulate the securities market by such measures as it thinks fit and such measures may be for any or all of the matters provided in sub-section 2 of Section 11 of the Act. SEBI has power to pass interim orders and such interim orders can also be passed exparte. Interim orders are passed in order to prevent further possible mischief of tampering with the securities market. If during a preliminary enquiry, it is found prima-facie, that the person is indulging in manipulation of the securities market, it would be obligatory for SEBI to pass an interim order or for that matter an ex- parte interim order in order to safeguard the interests of the investors and to maintain the integrity of the market. Normally, while passing an interim order, the principles of natural justice has to be adhered to, namely, that an opportunity of hearing is required to be given. Procedural fairness embodying natural justice is to be applied whenever action is taken affecting the rights of the parties. At times, an opportunity of hearing may not be pre-decisional and may necessarily have to be post-decisional especially*

> *where the act to be prevented is imminent or where action to be taken brooks no delay. Thus, pre-decisional hearing is not always necessary when ex-parte ad-interim orders are made pending investigation or enquiry unless provided by the statute. In such cases, rules of natural justice would be satisfied, if the affected party is given a post-decisional hearing.*
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> *14. However, it does not mean that in every case, an ex-parte interim order should be passed on the pretext that it was imminent to pass such interim order in order to protect the interest of the investor or the securities market. An interim order, however, temporary it may be, restraining an entity/person from pursuing his profession/trade may have substantial and serious consequences which cannot be compensated in terms of money.*
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> *15. Thus, ex-parte interim order may be made when there is an urgency. As held in* ***Liberty Oil Mills & Ors. vs. Union of India & 18 Ors. [AIR (1984) SC 1271] decided on May 1, 1984****, the urgency must be infused by a host of circumstances, viz. large scale misuse and attempts to monopolise or corner the market. In the said decision, the Supreme Court further held that the regulatory agency must move quickly in order to curb further mischief and to take action immediately in order to instill and restore confidence in the capital market."*

8. The aforesaid decision is fully applicable in the instant case and the reasoning given therein are not being repeated. In the instant case, we find that the trades were executed in October 2016. The investigation started in 2017 and continued till 2019 and, during this period, there was no shred of any evidence to suggest that the appellant was trying to divert the alleged notional gain.

9. We find that the only reason directing the appellant to deposit the alleged notional gain / loss in an Escrow Account is based on the finding given in paragraph 22 of the impugned order, namely, that "it is possible that the entity may divert the notional gain" and that if an interim order is not passed it would defeat the effective implementation of the disgorgement, if any, to be passed on merits after adjudication. In our opinion, the reasoning given by the WTM justifying its action to pass an ex-parte interim order is patently erroneous and cannot be sustained. On one hand, we find that only a show cause notice has been issued and the matter has not been adjudicated on merits but the appellant, on the other hand, has been directed to deposit the possible disgorgement amount in advance. We are of the opinion that no amount towards disgorgement can be directed to be deposited in advance unless it is adjudicated and quantified unless there is some evidence to show and justify the action taken. An order of the like nature can only be passed during the pendency of the proceedings and such orders cannot be passed at the time of initiation of the proceedings. Further, no order of the like nature can be passed without recording its satisfaction and cannot be based on the basis of possibility.

10. In this regard, we may refer to the provisions of Order 38 Rule 5 to 13 of the Code of Civil Procedure, 1908 which lays down the parameters for attachment before judgment. The said principles are fully applicable in the instant case. The object of attachment before judgment is to prevent any attempt on the part of the appellant to defeat the realization of the final order on disgorgement that may be passed against the appellant. But this principle applies only when it is found that the appellant is about to dispose of the property in question. Further, this principle can only be applied when there is evidence to show that the appellant has acted, or is about to act with the intent to obstruct or delay the adjudication of the proceedings that may be passed against him. We are of the opinion that there is no finding that the appellant will remove the property or will dispose of all the property or that he would obstruct the proceedings or that he would delay the proceedings pursuant to the show cause notice. In the absence of any such finding, the ex-parte interim order cannot be sustained especially when the trades were of 2016 and from 2016 till the date of the impugned order there is no evidence to show that the appellant was trying to divert the alleged notional gain/loss

11. As held in ***North End Foods Marketing Pvt. Ltd. (supra)*** there is no real urgency in the matter to pass an ex-parte interim order especially during the pandemic period. There is no doubt that SEBI has the power to pass an interim order and that in extreme urgent cases SEBI can pass an ex-parte interim order but such powers can only be exercised sparingly and only in extreme urgent matters. In the instant case, we do not find any case of extreme urgency which warranted the respondent to pass an ex-parte interim order only on arriving at the prima-facie case that the appellant was an insider as defined in the SEBI (Prohibition of Insider Trading) Regulations, 2015 ('PIT Regulations' for short) without considering the balance of convenience or irreparable injury.

12. In the light of the aforesaid, the impugned order cannot be sustained and the same is quashed at the admission stage itself without calling for a counter affidavit except the show cause notice. The appeal is allowed. The Misc. Application No. 154 of 2020 and Misc. Application No. 155 of 2020 are accordingly disposed off. We further direct that the appellant to file a reply to the show cause notice within four weeks from today. The respondent will decide the matter finally after giving an opportunity of hearing to the appellant either through physical

hearing or through video conference within six months thereafter. During the interim period, in order to safeguard the interests of the respondent and more particularly the interest of the investors in the securities market and also to protect the integrity of the securities market, we direct the appellant to give an undertaking to the respondent within four weeks from today that he will not alienate 50% of his total shareholdings of the company DTL held as on date, as stated by the learned counsel for the appellant. In the circumstances of the case parties shall bear their own costs.

13. The present matter was heard through video conference due to Covid-19 pandemic. At this stage it is not possible to sign a copy of this order nor a certified copy of this order could be issued by the registry. In these circumstances, this order will be digitally signed by the Presiding Officer on behalf of the bench and all concerned parties are directed to act on the digitally signed copy of this order. Parties will act on production of a digitally signed copy sent by fax and/or email.

Sd/-
Justice Tarun Agarwala
Presiding Officer

Sd/-
Dr. C.K.G. Nair
Member

Sd/-
Justice M.T. Joshi
Judicial Member

27.06.2020
msb