

THE TAKEOVER CODE: A COMPREHENSIVE OVERVIEW

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INTRODUCTION

Takeover of a listed company is not all about the target company being keen to get the highest possible price for its shares, while the acquirer going for the least possible financial and regulatory burden, rather it has *impact* on a host of stakeholders, such as, the acquirer, the target company, the management and the public shareholders. So, a precise, fair, unambiguous, equitable, transparent and predictable legal framework is desirable for balancing multiple, and at times, conflicting interests of stakeholders. Regulating the substantial acquisition of shares, in an organized manner and takeover of a company, whose shares are listed on a stock exchange is the legislative intention behind framing of Takeover code (herein after referred as *the code*). Before uncodifying the code and entering into the discussion of evolution of takeover laws and how the system works it is important to know what takeover is.

Five people have six views. Though there is no universal definition of takeover but the definition given by M.A. Weinberg is close to the concept accepted in legal regime. He defined takeover as “a transaction or series of transactions whereby a person (individual, groups of individuals or company) acquires control over the assets of a company, either directly by becoming the owner of those assets or indirectly by obtaining control of the management of the company. Where shares are closely held (i.e. by a small number of persons), a takeover will generally be effected, by agreement with the holders of the majority of the share capital of the company being acquired. Where the shares are held by the public generally, the takeover may be effected, (1) by agreement between the acquirer and the controllers of the acquired company; (2) by purchase of a on the Stock Exchange; or (3) by means of a ‘takeover bid’”.¹

Evolution

The concept of takeover first emerged in the late 19th century in US, UK and other countries when the first wave of mergers and acquisitions (herein after referred as M & A) bulged out. In India, incorporation of Clause 40 of the listing agreement was the first attempt to regulate takeovers. Making a public offer to the shareholders of a company was made mandatory if

¹ Sampath K.R., Law and Procedure for Mergers/Joint Ventures Amalgamations Takeovers & Corporate Restructure, 4th ed., 2008, Snow White Publications Pvt. Ltd., Mumbai. p. 619.

the acquisition of shares or voting right exceeds 25%. However, acquiring the voting rights a little below the threshold limit of 25% for making a public offer baffled the very design of the regulation. Thence, the threshold limit was reduced to 10% in 1990. Subsequently, Clause 40A and 40B of the Listing Agreement were introduced to meet the need to make a public offer to acquire shares if there is a change in the management control, notwithstanding there being no change in the shareholding. These measures were introduced with an intention to help the process of acquisition of shares and takeovers transparent and providing for protection of investors' interests. But limited applicability and weak enforceability didn't effectuate desired results. Moreover, the Listing Agreement was a contractual obligation between companies whose shares were listed on a Stock Exchange and the punishment for non-compliance was the delisting of the company's shares which in fact turned out to be antithetical to the welfare of the investors, which is intended to be protected.

The SEBI Act 1992 authorized SEBI to regulate substantial acquisition of shares and takeovers and also granted the right to instigate criminal prosecution, issue guilty person direction not to further deal in securities, forbid him from disposing of any securities acquired in violation of the regulations, or direct him to sell shares acquired in violation of the Regulations and take action against the concerned intermediary who is registered with SEBI. Subsequently, *the SEBI substantial acquisition of shares and takeovers regulations, 1994* came, which remained in force till 20th February, 1997 when revised *SEBI substantial acquisition of shares and takeovers* was notified.

The Regulations was framed under Section 30 of the Securities Exchange Board of India Act, 1992 in light of the recommendations of the first Bhagwati Committee's report of January 18, 1997. The 1997 Takeover Code underwent further amendments in light of the recommendations made by the second Bhagwati Committee's report² and the SEBI Substantial Acquisition of Shares and Takeovers (Second Amendment) Regulations, 2002 came with effect from September 9, 2002.

Purpose and Scope of the Code

Before discussing the code in details let us have a glance on the legislative intention behind passing this law and the scope there of. The purpose of takeover regulations is to provide transparency arising out of substantial acquisition of shares and takeovers and to bring

² The report was submitted in May 2002.

fairness in such transactions so as to protect the interest of the investors in securities. The Code also protects the interests of small shareholders so that in any substantial acquisition of shares, they get a fair price for the shares transferred by them. In the case of *K.K. Modi v. SAT*,³ the Court categorically stated that the code has been framed with a view to protect the interests of investors in securities and to promote development of and to regulate the securities market and for matters connected therewith or incidental thereto.

The code has a limited role and is not meant to ensure proper management of the business of companies or to provide remedies in the event of mismanagement. Securities Appellate Tribunal has observed that the main objective of the code is to ensure quality of treatment of opportunity to all shareholders and afford protection to them.⁴

³ (2002) 35 SCL 230 Mum.

⁴ Punjab State Industrial Corporation Ltd. v. SEBI, (2001) 32 SCL 631 Mum.

SEBI REGULATIONS AND THE BHAGWATI COMMITTEE REPORTS

To protect the interest of investors, promote the development of the securities market and regulate substantial acquisitions of shares and takeovers, the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 have been drafted by SEBI under its mandate. The said Regulation of 1997 is referred to as Takeover Code and is applicable to acquisition of shares of all listed companies. It defines some of the important terms which are pertinent to the discussion on the issue of takeover. Following are some of the regulations with reference to the Bhagwati Committee report.

Regulation 2 of the Code has the definition clauses and Sub-regulation (b) defines “acquirer” as follows:

any person who, directly or indirectly, acquires or agrees to acquire shares or voting rights in the target company, or acquires or agrees to acquire control over the target company, either by himself or with any person acting in concert with the acquirer;

Regulation 2(e) defines "Person acting in concert" which comprises: persons who, for a common objective or purpose of substantial acquisition of shares or voting rights or gaining control over the target company, pursuant to an agreement or understanding (formal or informal), directly or indirectly co- operate by acquiring or agreeing to acquire shares or voting rights in or control over the target company. Paragraph 2 of the said regulation gives a list of persons who will be deemed to be persons acting in concert with other persons in the same category, *unless the contrary is established* (emphasis added):

- i. a company, its holding or subsidiary company or company under the same management either individually or together with each other;
- ii. a company with any of its directors, or any person entrusted with the management of the funds of the company;
- iii. directors of companies and their associates;
- iv. mutual fund with sponsor or trustee or asset management company;
- v. foreign institutional investors with sub-account(s);
- vi. merchant bankers with their client(s) as acquirer;
- vii. portfolio managers with their client(s) as acquirer;
- viii. venture capital funds with sponsors;

- ix. banks with financial advisers, stock brokers of the acquirer, or any company which is a holding company, subsidiary or relative of the acquirer⁵
- x. any investment company with any person who has an interest as director, fund manager, trustee, or as a shareholder having not less than 2 per cent of the paid-up capital of that company or with any other investment company in which such person or his associate⁶ holds not less than 2 per cent of the paid-up capital of the latter company.

Chapter II of the Code deals with "Disclosures of Shareholding and Control in a Listed Company" and Chapter III contain provisions dealing with "Substantial Acquisition of Shares or Voting Rights in and Acquisition of control over a Listed Company". Chapter III begins with **Regulation 10** that makes it **obligatory** for an "acquirer" acquiring, in aggregate, *fifteen percent or more* of the voting rights in a company whether by acquisition of shares or voting rights *to make a public announcement to acquire shares of that company* in accordance with the provisions of the Takeover Regulations (emphasis added).

Regulation 11 deals with "Consolidation of holdings", which lays down certain obligations of an "acquirer" who, together with persons acting in concert with him, has acquired 15% or more but less than 55% of the shares or voting rights in a company.

At the end of Regulation 11 there is an explanation that applies both to Regulations 10 and 11. The explanation says that the acquisition shall mean and include- *direct* acquisition in a listed company to which the regulations apply and *indirect* acquisition by virtue of acquisition of companies, whether listed or unlisted, whether in India or abroad.

Regulation 14 prescribes the *time limit* within which the public announcement stipulated in Regulation 10 is to be made. The public announcement shall be made by the merchant banker *not later than four working days of* entering into an agreement for

⁵ Provided that Sub-clause (ix) shall not apply to a bank whose sole relationship with the acquirer or with any company, which is a holding company or a subsidiary of the acquirer or with a relative of the acquirer, is by way of providing normal commercial banking services or such activities in connection with the offer such as confirming availability of funds, handling acceptances and other registration work.

⁶ The clause "associate" means,--(a) any relative of that person within the meaning of Section 6 of the Companies Act, 1956 (1 of 1956); and (b) family trusts and Hindu undivided families.

acquisition of shares or voting rights or deciding to acquire shares or voting rights exceeding the respective percentage specified therein.⁷

Sub regulation 2 says in the case of an acquirer acquiring securities, including Global Depository Receipts or American Depository Receipts which, when taken together with the voting rights, if any already held by him or persons acting in concert with him, would entitle him to voting rights, exceeding the percentage specified in regulation 10 or regulation 11, the public announcement referred to in sub-regulation (1) shall be made *not later than four working days* before he acquires voting rights on such securities upon conversion, or exercise of option, as the case may be⁸.

Sub regulation 3 prescribes that the public announcement referred to in Regulation 12 shall be made by the merchant banker *not later than four working days* after any such change or changes are decided to be made as would result in the acquisition of control over the target company by the acquirer.

Sub regulation 4 deals with **indirect acquisition** or change in control and provides that a public announcement shall be made by the acquirer *within three months* of consummation of such acquisition or change in control or restructuring of the parent or the company holding shares of or control over the target company in India.

The problem as to the time allowed for making the public announcement was considered by the **second Bhagwati Committee**. The Committee observed that indirect acquisition of a company is done through chain principle. The public offer for the company which gets acquired as a consequence of the takeover of the target company is triggered only upon the successful completion of the acquisition of the target. At the time of making the offer for the target company, such a takeover or rather its success is contingent and prospective and in the event of its failure, the consequent offer does not arise. Though the public announcement for the consequent offer could be made simultaneously, it would be

⁷ Provided that in case of disinvestment of a Public Sector Undertaking, the public announcement shall be made by the merchant banker not later than 4 working days of the acquirer executing the Share Purchase Agreement or Shareholders Agreement with the Central Government or the State Government as the case may be, for the acquisition of shares or voting rights exceeding the percentage of shareholding referred to in regulation 10 or regulation 11 or the transfer of control over a target Public Sector Undertaking.

⁸ Provided that in case of American Depository Receipts or Global Depository Receipts entitling the holder thereof to exercise voting rights in excess of percentage specified in regulation 10 or regulation 11, on the shares underlying such depository receipts, public announcement shall be made within four working days of acquisition of such depository receipts.

conditional upon the successful completion of the first offer. Such conditional offer has its own impact on the market and is not without practical and procedural difficulties. Hence the public announcement for the consequent offer can be allowed to be made within a pre-specified time period of three months from the date of closure of the first offer. So, the Committee recommended that:

The offer for a company which gets acquired as a result of acquisition of a target company can be subsequent to the successful completion of the takeover of the target by the acquirer. It should be made within 3 months of consummation of restructuring or arrangement by parent or holding company.

In pursuance of the recommendation of the second Bhagwati Committee's report, Sub-Regulation (4) got inserted in regulation 14.

Regulation 16 deals with the "Contents of the public announcement of offer" and importantly clause (ix) provides for the **object and purpose** of the acquisition of the shares and future plans, if any, of the acquirer for the target company.

The concept of "offer price" is dealt under **Regulation 20**. The offer to acquire shares under Regulation 10, 11 or 12 shall be made at a price not lower than the price determined as per Sub-regulations (4) and (5). Sub-regulation (4) says that the offer price shall be the highest of:

- a) the negotiated price under the agreement referred to in Regulation 14 (1);
- b) price paid by the acquirer or persons acting in concert with him for acquisition, if any, including by way of allotment in a public or rights or preferential issue during the twenty-six week period prior to the date of public announcement, whichever is higher;
- c) the average of the weekly high and low of the closing prices of the shares of the target company as quoted on the stock exchange where the shares of the company are most frequently traded during the twenty-six weeks or the average of the daily high and low of the prices of the shares as quoted on the stock exchange where the shares of the company are most frequently traded during the two weeks preceding the date of public announcement, whichever is higher⁹.

⁹ Provided that the requirement of average of the daily high and low of the closing prices of the shares as quoted on the stock exchange where the shares of the company are most frequently traded during the two weeks preceding the date of public announcement, shall not be applicable in case of disinvestment of a Public Sector Undertaking.

Sub-regulation (5) provides that where the shares of the target company are infrequently traded, the offer price shall be determined by the acquirer and the merchant banker taking into account the following factors:

- a) the negotiated price under the agreement referred to in Regulation 14(1);
- b) the highest price paid by the acquirer or persons acting in concert with him for acquisitions, if any, including by way of allotment in a public or rights or preferential issue during the twenty-six week period prior to the date of public announcement;
- c) other parameters including return on net worth, book value of the shares of the target company, earning per share, price earning multiple vis-a-vis the industry average: Provided that where considered necessary, the Board may require valuation of such infrequently traded shares by an independent merchant banker (other than the manager to the offer) or an independent chartered accountant of minimum ten years' standing or a public financial institution.

The **second Bhagwati Committee** recommended for a separate and extended time period for making the public offer for a company that gets taken over following the acquisition of a target company. The Committee had in mind that the extended period for making the public offer does not act to the detriment of the ordinary shareholders of the company that gets taken over as a result of acquisition of a target company. The Committee recommended that:

The price shall be determined as highest of the two prices determined as per the provisions of the Regulations, with reference to the date of the public announcement for the target company and the date of public announcement for the company which is consequently acquired.

Regulation 20(12), which came after this recommendation plainly says that the offer price for the shares of a company being taken over indirectly and as a consequence of the acquisition of the primary target, would be determined with reference to two dates, one when the public offer was made in regard to the "Parent company" and the other when the public offer is made for the secondary target company and the higher of the two will be taken as the offer price.

REPORT OF THE TRAC

The growing level of M&A in India and the increasing sophistication of takeover market made it necessary to review the Takeover Regulations of 1997. So, SEBI¹⁰ constituted the Takeover Regulations Advisory Committee (TRAC) with the mandate to examine and review the Takeover Regulations of 1997 and to suggest suitable amendments. The committee, headed by Mr. C. Achuthan, submitted its report to SEBI on July 19, 2010.

Objectives

The fundamental objectives of the TRAC committee were to provide a fair, equitable and transparent legal framework for facilitating takeover activities. To balance the conflicting objectives and interests of various stakeholders in the case of substantial acquisition of shares in, and takeovers of, listed companies is another aim of the TRAC report. To ensure that fair and accurate disclosure of all material information is made by persons responsible for making them to various stakeholders to enable them to take informed decisions and to ensure that only those acquirers who are capable of actually fulfilling their obligations under the Takeover Regulations, make open offers were some of the objectives sort to achieve by this report.

Comparison between the Current Regulations and the Committee Recommendations

The comparison between the current provisions regulating takeover and the proposed recommendations by the TRAC is highlighted below.

Open Offer Obligation

The Takeover Regulations essentially require an open offer to be made by an acquirer acquiring substantial stake in or control of a listed company so as to provide the existing shareholders an exit opportunity in case they do not have confidence in the likely new management of the company.

Initial Trigger: The Takeover Regulations currently provide that if an acquirer acquires or agrees to acquire shares or voting rights such that his voting rights exceed 15 % of the voting capital of the target company, he is required to make an open offer.¹¹

¹⁰ Vide its order dated September 4, 2009.

¹¹ Regulation 10 of the SEBI (SAST) Regulations, 1997

The committee recommended that acquisitions of an aggregate of 25% or more voting rights in a target company would require the acquirer to make an open offer.¹² So, the committee has increased the aggregate voting right by 10%.

The TRAC has examined the shareholding pattern of listed companies in India and arrived at the conclusion that the earlier threshold was fixed in an environment where the shareholding pattern of companies in India was such that it was possible to control listed companies with holdings as low as 15%. The recommendation seems to be beneficial from the point of Private Equity and Institutional investors who had to restrict themselves to 14.99% stake in every listed company in terms of Existing Regulations as otherwise it would necessitate the Open Offer to the shareholders of the Target Company for which they are in no way interested to do as their objective is not to acquire the control over the company. However, it is apprehended that the increase in threshold would reduce the number of open offers and hence might be viewed negatively from the point of view of small shareholders.¹³

Creeping Acquisition Trigger: The Takeover Regulations currently provide that if an acquirer already holds more than 15 % but less than 55 %, he may acquire additional shares carrying *not more than 5 %* of voting rights within a financial year without making an open offer.¹⁴

Secondly, where the Acquirer together with the person acting in concert with him holds 55% or more but less than 75% shares, then he *cannot acquire even a single share* without making public Announcement to the shareholders of the Target Company.¹⁵ However, the second proviso of the sub Regulation gives one-time allowance to the Acquirer with PACs to increase their shareholding by 5% through market purchases in normal segment or pursuant to a Buy back by the target company, without having to make an open offer provided that post acquisition holding of acquirer does not go beyond 75%. Further, it is to be noted that irrespective of the level of minimum public shareholding required to be maintained in terms of Clause 40A of the listing agreement, the total shareholding of acquirer along with the PAC consequent to the creeping acquisition as allowed under second proviso to regulation 11(2) should not increase beyond 75%.

It is recommended by the committee that promoters who own more than 25% of voting rights may **buy up to 5%** of the company's shares every year, through a creeping

¹² See Regulation 3(1), the TRAC report.

¹³ The Takeover Panorama, Corporate Professionals, Year IV-vol. XI, November, 2010.

¹⁴ Regulation 11(1) of the SEBI (SAST) Regulations, 1997.

¹⁵ Id., Regulation 11(2).

acquisition, up to a maximum of 75%, without making a Public Announcement.¹⁶ Further, it is provided that the Acquirer shall not enter into an agreement to acquire any shares which will increase his shareholding beyond the maximum non-public shareholding limit i.e. 75%. Thus Clause 40A of the listing agreement should not be breached by the Acquirer.¹⁷ In the TRAC Report, the provisions of Regulation 11(1) and 11(2) of SEBI (SAST) Regulations, 1997 have been merged and incorporated in regulation 3(2) with some modifications.

Control Trigger: The Takeover Regulations provide that if any acquirer (including person acting in concert) acquires control over the target company irrespective of the fact whether there has been any acquisition of shares or not, he has to give public announcement to acquire shares from shareholders of the Target Company. However, *the requirement of public offer is not applicable if the shareholders of the company approve the change in control by way of a Special Resolution.* Furthermore the Regulation also provides the facility of voting *through postal ballot* to the shareholders of the Company for passing of the special resolution. It is appreciable that the acquisition of control also includes both direct & indirect acquisition of control over Target Company by virtue of acquisitions of companies whether listed or unlisted.¹⁸

Regulation 4 of the TRAC Report specifies that if any acquirer (including person acting in concert) acquires control over the Target Company irrespective of the fact whether there has been any acquisition of shares or not, he has to give public announcement to acquire shares from shareholders of the Target Company. However, *the exemption from open offer available in case of change in control without acquisition of substantial shares, through a special resolution by postal ballot process, has been **withdrawn***¹⁹ and now the only route available for change in management and control is through the Open Offer to the shareholders of the Target Company.

Indirect Acquisitions

The Takeover Regulations currently provide that acquirer has to make an open offer for shares of the target company when there is direct or indirect change of control of the target company irrespective of any direct acquisition of shares of the target company.

¹⁶ See Regulation 3(2), the TRAC report.

¹⁷ Id.

¹⁸ See Regulation 12 of the SEBI (SAST) Regulations, 1997.

¹⁹ This provision is in contrast with the Regulation 12 of the existing SEBI Takeover Regulations which provides for the change in control through the special resolution passed by way of postal ballot.

The Committee recommended that irrespective of whether the target company is material to the parent transaction, open offer obligations have to be triggered. Where a change in control over the target company occurs, shareholders of the target company ought to rightfully get an adequate exit opportunity.²⁰

Voluntary Open Offer

Currently, the Takeover Regulations provide for consolidation of shareholding by an acquirer, who is desirous of maximizing his shareholding without breaching the minimum public shareholding requirements. The offer size for an open offer under this provision is the lower of 20% or the maximum permissible acquisition without breaching the minimum public shareholding requirement.

The committee recommended that Shareholders holding shares entitling them to exercise 25% or more of the voting rights in the target company may, without breaching minimum public shareholding requirements under the listing agreement, voluntarily make an open offer to consolidate their shareholding.²¹

Offer Size

The Regulations currently require that on acquisitions resulting in triggering regulations 10, 11 and 12, the acquirer is mandatorily required to make an open offer for a minimum of 20% of the voting capital.

Considering several aspects including sound conceptual underpinnings, international best practices and feedback from the public the Committee has concluded that there is a very strong case for allowing *all* public shareholders to obtain a *complete* exit whenever an open offer is made. Therefore any open offer under the Proposed Takeover Regulations would be for 100%, i.e., for all the shares held by all the other shareholders of the target company.²²

Exemption from open offer obligations

Exemptions available from the applicability of the regulations are of two types viz. automatic exemptions, which do not require approval or confirmation from SEBI and second is a set of exemptions, which require prior approval of SEBI. The Takeover Regulations currently provide for fourteen categories of transactions which are exempted from the requirement to

²⁰ See Regulation 5, the TRAC report.

²¹ Id., Regulation 6.

²² Id., Regulation 7(1).

make an open offer subject to satisfying the conditions specified therein, if any, without the need to seek SEBI's approval for the same. Further, for the transactions that are not covered in the aforesaid fourteen categories, an application can be made for seeking exemption from SEBI. Such applications are referred to a "takeover panel" for its recommendations. SEBI considers the recommendations received and passes an appropriate order.

It is recommended by the committee that the SEBI would continue to have the power to grant exemption from making an open offer. However, *the requirement of making a mandatory reference to a Panel by SEBI before granting an exemption has been done away with* and such requirement has now been made discretionary.²³

Offer Price

The Takeover Regulations currently provide the parameters to be considered for determining the minimum offer price depending on whether or not the shares of the target company are frequently traded. Such parameters for frequently traded shares include the price under the agreement for acquisition that attracted the open offer, any price paid by the acquirer or persons acting in concert during a 26-week period preceding the public announcement (look back period), and the historical market average price of the shares for a proximate past period. For infrequently traded shares, the Takeover Regulations require the computation of the offer price on the basis of financial parameters such as return on net worth, industry price-earnings multiples and the like, apart from any price actually paid by the acquirer or persons acting in concert during the look back period, or in the transaction that triggers the open offer obligation. The Takeover Regulations also require addition to the open offer price, of any amount paid towards non-compete fee in excess of 25 % of the open offer price.

The committee recommended that the minimum price payable as the offer price continues to be regulated and shall be the highest of:

- the negotiated price under the agreement that attracted the open offer;
- volume-weighted average price paid by the acquirer and persons acting in concert in the preceding fifty-two weeks;
- highest price paid by the acquirer or persons acting in concert with him during the preceding twenty-six weeks;

²³ Id., Regulation 11.

- sixty trading day volume weighted average market price (for frequently traded shares).

To compute the offer price for indirect acquisitions, in addition to the above parameters, any higher price paid during the period between contracting of the primary transaction and the public announcement has also to be considered. In case of indirect acquisitions of the target company, the offer price would stand increased at the rate of 10% per annum calculated on a pro-rata basis for the period from the date of the primary transaction being announced in the public domain until the date of actual detailed public statement in respect of the target company. Such revised offer price shall be payable to all shareholders who tender their shares in the open offer.²⁴

Mode of payment

The Takeover Regulations currently provide that offer consideration shall be payable either (a) by way of cash; (b) by issue, exchange and, or transfer of shares (other than preference shares) of acquirer company, if the person seeking to acquire the shares is a listed body corporate; or (c) by issue, exchange and, or transfer of secured instruments of acquirer company with a minimum 'A' grade rating from a credit rating agency registered with the Board; or (d) a combination of clause (a), (b) or (c).

The committee recommended that the offer price may be paid in the form of cash or securities like shares, convertibles, secured debt instruments of the acquirer or of persons acting in concert with him or a combination of these modes. To ensure that the equity shares given in consideration for the open offer are liquid, eligibility conditions have been stipulated. However, if shares of the target company carrying more than 10% voting rights have been acquired for cash in the preceding 52 weeks, shareholders to whom the open offer is made may opt to receive the offer price only in cash.²⁵

Withdrawal of open offer

The Takeover Regulations currently provide that *no open offer shall be withdrawn except-* (a) the statutory approval(s) required have been refused;
(b) the sole acquirer, being a natural person, has died;
(c) such circumstances as in the opinion of SEBI merits withdrawal

²⁴ Id., Regulation 8.

²⁵ Id., Regulation 9.

The Committee recommended that, in addition to the grounds currently existing, an open offer may be withdrawn where *any condition stipulated in the agreement for acquisition attracting the obligation to make the open offer is not met* for reasons outside the reasonable control of the acquirer, and such agreement is rescinded, subject to such conditions having been disclosed in the detailed public statement and the letter of offer.²⁶

Obligations of the Acquirer and the Target Company

The Takeover Regulations currently provides that where the acquirer has not stated his intention to dispose of or otherwise encumber any assets of the target company except in the ordinary course of business of the target company, the acquirer shall be debarred from disposing of or otherwise encumbering the assets of the target company for a period of 2 years from the date of closure of the public offer.

The Committee recommended that unless acquirer has declared an intention in the detailed public statement and the letter of offer, the acquirer shall be debarred from alienating any material assets of the target company (including its subsidiaries) for a period of two years after the offer period. However, where such alienation is necessary despite no such intention having been expressed by the acquirer, the target company shall require a special resolution passed by the shareholders by way of a postal ballot.²⁷

Similarly, the Takeover Regulations currently provide that the target company *shall not*, during the offer period sell, transfer, encumber or otherwise dispose of assets of the company or its subsidiaries or enter into any material contracts.

The Committee recommended retaining restrictions on the target company during the offer period from carrying out material transactions outside the ordinary course of business *except* with the consent of the shareholders through a special resolution and the same rule would apply to the subsidiaries of the target company.²⁸

Obligations of the Merchant Banker

The Takeover Regulations currently provide that the merchant banker shall *ensure compliance* of the Takeover Regulations and any other laws or rules as may be applicable in this regard and provide other specific obligations under Regulations 24 of the current Takeover Regulations.

²⁶ Id., Regulation 23.

²⁷ Id., Regulation 25.

²⁸ Id., Regulation 26.

The Committee recommended that the merchant banker would be expected to *demonstrate the application* of due skill, care and diligence in the discharge of professional duties cast on him and the obligations of the merchant banker ought to be construed accordingly.²⁹

Composition of the Board

The Takeover Regulations currently provide that till the offer formalities are completed, the target company *shall be precluded* from inducting any person or person nominated by the acquirer or belonging to his group into the board of the target company (except in cases, where acquirer deposits full consideration in an escrow account).

The Committee recommended that the acquirer or persons acting in concert with him *may be represented on the board only after* the expiry of a period of 15 business days from the date of the detailed public statement and provided the entire consideration payable under the open offer is deposited in cash in the escrow account required under the Takeover Regulations and the offer is not subject to any conditions other than regulatory approvals.³⁰ By making this recommendation, the Committee has given opened the prohibited gate for the acquirer or person related to it to enter into the board of the target company.

Recommendation by the independent directors of the Target Company

The Takeover Regulations currently provide that the board of directors of the target company *may*, send their unbiased comments and recommendations on the offer(s) to the shareholders.

The Committee recommended that the independent directors on the board of directors of the target company *ought to* make a reasoned recommendation on the open offer and for such a recommendation, the board of the target company ought to appoint a committee of independent directors.³¹

Disclosure Obligations

The current Takeover Regulations obligate any acquirer who crosses the specified thresholds to disclose *at every stage* his aggregate shareholding or voting right to the company concerned and to the stock exchanges where shares of the company are listed. The promoter

²⁹ Id., Regulation 27.

³⁰ Id., Regulation 24.

³¹ Id., Regulation 26 (6).

or majority shareholder is under an obligation to disclose to the company and the concerned stock exchange *annually*.

The Committee recommended that the acquirer promoter/shareholders shall be asked to disclose their acquisition on *periodic* as well as *transaction specific basis* upon crossing the limits specified therein to the Stock Exchange.³²

³² Id., Regulation 28.

JUDICIAL PRONOUNCEMENTS

Daiichi Sankyo company Ltd. v. Jayaram Chigurupati and Ors.

The judgment delivered in Daiichi Sankyo Company Ltd. v. Jayaram Chigurupati and Ors.³³, which was the common judgment for both the appeals³⁴, is an important case relating to the issues of indirect takeover. The facts of the case are as follows:

Facts:

On October 3, 2007 **Ranbaxy Laboratories Limited** entered into a Share Purchase and Share Subscription Agreement (herein after referred to as SPSSA) to purchase from Zenotech's promoter 78,78,906 shares (27.35% of the company's fully paid-up equity share capital) at the negotiated price of Rs. 160.00 per equity share and to subscribe to 54,89,536 fully paid-up equity shares at the same price under a preferential allotment by Zenotech.

So, Ranbaxy was legally obliged to make a public announcement to acquire shares of the company from the ordinary shareholders, as the share holding is more than 15%. In the public announcement it sought to acquire from the shareholders, equity shares of Zenotech constituting 20% of its expanded share capital with the quoted offer price of Rs. 160.00 per equity share. On November 8, 2007 the share purchase transaction between Ranbaxy and Zenotech was completed and the shareholders of Zenotech approved the preferential allotment and on November 23, 2007 Zenotech preferentially allotted 54, 89,536 fully paid-up shares to Ranbaxy. Up to this stage Daiichi was nowhere on the scene.

On June 11, 2008 Daiichi entered into a SPSSA jointly with (i) Malvinder Singh and others, the promoters of Ranbaxy, and (ii) Ranbaxy Laboratories Ltd. to acquire 30.91% of the fully paid-up equity share capital of Ranbaxy. In addition, Daiichi would subscribe to shares, representing 11% of the fully paid-up equity share capital of Ranbaxy, and 2, 38, 34,333 share warrants. On the same day Ranbaxy informed the Stock Exchanges that since Ranbaxy was holding 46.85% of the equity shares of Zenotech, the SPSSA "has also triggered an 'Open Offer' to be made by Daiichi to the public shareholders of 'Zenotech' to acquire a minimum of 20% of the Equity Shares of 'Zenotech' at a price to be determined under the SEBI Regulations".

³³ AIR2010SC3089, [2010]157CompCas380(SC), [2010]103SCL1(SC), 2010(6)UJ3002(SC).

³⁴ Civil Appeal No. 7148 of 2009 and Civil Appeal No. 7314 of 2009.

On June 16, 2008 it made a public announcement to the shareholders of Ranbaxy to acquire in the aggregate 22.01% of the fully paid-up equity share capital of Ranbaxy. The offer price in the public announcement was Rs. 737.00 for each share. Daiichi's control over Ranbaxy consummated on October 20, 2008 when it acquired more than 50% of the share capital of Ranbaxy and on and from that date Ranbaxy became a subsidiary of Daiichi.

As a result of its takeover of Ranbaxy, Daiichi also acquired control of 46.85% of the equity share capital in Zenotech, held by Ranbaxy. Daiichi made the public announcement to the shareholders of Zenotech with the offered price of Rs. 113.62 for each share of Zenotech. In regard to the offer price a complaint to SEBI was filed. The SEBI after due consideration of the matter turned down the claim of the respondents.

Against the decision of the SEBI, the complainant preferred separate appeals before the Security Appellate Tribunal (SAT). *The SAT upheld the claim of the respondents and reversed the decision of the SEBI*, and directed Daiichi to offer Rs. 160.00 per share to the shareholders of Zenotech. Daiichi then brought the matter in appeal before the Supreme Court.

Issues:

1. Whether the offer price for the shares of Zenotech by Daiichi is in accordance with the code?
2. Whether Daiichi Sankyo and Ranbaxy could be considered as 'person acting in concert'?

Decision:

The period of time within which Daiichi was required to make the public announcement in respect of both companies were prescribed in Sub-regulation (1)³⁵ and (4)³⁶ respectively of Regulation 14. It was observed by the court that Sub-regulation (4) was inserted in Regulation 14 by the Second Amendment Regulation 2002 which means that prior to that the time limit was *four days for making the public announcement for both direct and indirect acquisitions*. In terms of Regulation 20(12) the **share price** of Zenotech was required to be

³⁵ Not later than four working days of entering into an agreement for acquisition of shares or voting rights.

³⁶ Within three months of consummation of such acquisition or change in control.

determined as on June 16, 2008 (the date of the public announcement for Ranbaxy) and as on January 19, 2009 (the date of the public announcement for Zenotech).

Regulation 20(12) tells us the dates with reference to which the offer price is to be determined but it does not tell us how the offer price is to be determined. For that reference is made to Sub-regulations (4) and (5) and Regulation 20(12) jointly. According to Daiichi, Regulation 20(4)(a) had no application in determining the offer price of Zenotech as there was no negotiated price under any agreement. Similarly, Regulation 20(4)(b) had no application because neither Daiichi nor anyone acting in concert with it had purchased any shares of Zenotech within the period of 26 weeks prior to the dates of the two public announcements (i.e. for Ranbaxy and Zenotech). The only provisions, therefore, applicable in the case were those contained in Clause (c) of Regulation 20(4) under which the **offer price was required to be determined on the basis of prices of the shares of Zenotech**. The appellant worked out the share price of Zenotech as on June 16, 2008 and January 19, 2009, following the different modes provided under Regulation 20(4)(c) and, in the public announcement, offered Rs. 113.62 per share, that being the **highest among all**, which was agreed by the respondents. But the respondents contended that Clause (b) of Regulation 20(4) is attracted and the price Rs. 160.00 under that clause being higher than the price Rs. 113.62 worked out in terms Clause (c) that alone could form the offer price in the public announcement. The offer price in the public announcement for Zenotech shares made by the appellant was correctly worked out.

The SAT had accepted the respondents' contention holding that Ranbaxy became its subsidiary on October 20, 2008 when the acquisition of Ranbaxy got completed. The Tribunal also held that being a subsidiary, Ranbaxy shall be deemed to be acting in concert. But the counsel appearing on behalf of the appellant contended that the SAT grossly erred in holding that *the date of the public offer and the price paid for acquisition of Zenotech shares*, when the two companies were indisputably not in the relationship of "persons acting in concert" would be relevant **for determining the offer price** for Zenotech shares. Ranbaxy indeed became a subsidiary of Daiichi from October 20, 2009 but it did not acquire any share of Zenotech after that date. Any acquisition of Zenotech shares made by Ranbaxy earlier at a time when it was not a "person acting in concert" with Daiichi was of no consequence and the price paid by Ranbaxy for Zenotech shares at that time would certainly not attract Regulation 20(4) (b) of the Takeover Regulations.

The court held that there are no 'Persons Acting in Concert'³⁷ in relation to the offer and the judgment of the SAT was based on a complete **misinterpretation of the expression "person acting in concert"**. The Tribunal erred in assuming that "being a subsidiary, Ranbaxy shall be deemed to be acting in concert with Daiichi" and it 'missed the true import of the words "unless the contrary is established" at the conclusion of Regulation 2(e)(2)'. The court held that the definition of a "person acting in concert" requires something more than the mere relationship of a parent company and a subsidiary company. The court supported the argument stating that *two or more persons may join hands together with the shared common objective or purpose of any kind but so long as the common object and purpose is not of substantial acquisition of shares of a target company they would not comprise "persons acting in concert"*. The idea of "persons acting in concert" is not about a fortuitous relationship coming into existence by accident or chance. The relationship can come into being only by design. As there is nothing in the facts of the case to show that Daiichi and Ranbaxy entered into the SPSSA for the common objective or purpose of substantial acquisition of shares or voting rights or control over Zenotech, the purchase of Zenotech shares by Ranbaxy cannot be said to be by a "person acting in concert" with Daiichi. It was held that the Appellate Tribunal was wrong. So, the appeals were allowed.

Premier Limited case³⁸

Facts:

PAL Peugeot Limited (Target Company) was a joint venture (JV) between Premier Limited (Entity) and Automobile Peugeot, France (Transferor). In 1999, the transferor withdrew itself from the JV and gifted its entire shareholding constituting 8,40,25,000 Equity Shares to the entity. Consequently the shareholding of the entity increased from 30.12% to 62.08% of the paid up capital of the Target Company. It was alleged that as the transfer was by way of gift and not as per pricing determined under Regulation 20 of the SEBI (SAST) Regulations, 1997, the entity could exercise more control than what it was entitled prior to the ceding of control and that the cessation of joint control to a single control has to be treated as change in control. It was further alleged that the said acquisition was made without making Public Announcement resulting into the violation of Regulation 11(1), 12 and 14(1) of the SEBI (SAST) Regulations, 1997.

³⁷ See Regulation 2(1)(e)(1) of the SAST Regulations, 1997.

³⁸ Order of SEBI, WTM/KMA/CFD/307/10/2010.

It was contented that the Regulation 11(1) would not be applicable as it had not acquired any shares or voting rights in respect of the shares gifted to it and that the said shares are still in the name of the transferor. Mere execution of the share transfer deed by the transferor cannot amount to an acquisition or an agreement to acquire those shares unless such transfer deeds are signed by the transferee and lodged with the Company for registration of the transfer. However, the entity has not even signed the said transfer deed or lodged them for transfer with the Target Company.

Issue:

1. Whether the Noticee can be considered as Acquirer as defined in Regulation 2(1)(b) of the SEBI (SAST) Regulations, 1997?
2. Whether the Noticee is required to make Public Announcement under Regulation 11(1) and 12 of the SEBI (SAST) Regulations, 1997?

Decision:

Acceptance of the gift of share certificates and transfer deeds by the entity amounts to agreeing to acquire shares and the entity is an acquirer under the Regulation. In case of the acquisition of the voting rights, Section 150 of the Companies Act, 1956, specifies that a person holding shares with voting rights are entitled to exercise the voting right only on entering his name in the company's register of members. Therefore in view of the observations and the fact that the shares which has been gifted by the transferors still stand in its name, it can be concluded that the entity is not entitled to exercise voting rights in respect of the impugned shares and thus had not triggered Regulation 11(1) of SEBI (SAST) Regulations, 1997. Thus the matter is disposed off accordingly.

OCL India Limited³⁹

Facts:

The Appellants are the promoters of OCL India Limited (Target Company). The Target Company came out with Buy Back offer and declared that the promoters of the company would not participate in the offer. SEBI received a complaint from Jindal Securities Private Limited alleging that pursuant to the buyback offer the percentage of voting rights of the promoters got increased and they had violated the provision of Regulation 11 of the SEBI (SAST) Regulations, 1997. On examining the complaint, SEBI held that the promoters of the

³⁹ Order of SEBI, WTM/KMA/CFD/212/01/2011.

Target Company had violated the provision of Regulation 11 of the SEBI (SAST) Regulations, 1997, even though they did not actually acquire the shares. As per the SEBI, the mode of acquisition did not matter and since the promoters have acquired more than 5% of the voting rights, therefore, they should have made a Public Announcement. An Adjudicating Officer was appointed and while the adjudication proceedings was pending, the appeal was filed to SAT. While admitting the appeal, it was directed to the adjudicating officer to continue with the proceedings but not to pass any final order till the final disposal of the appeal.

Issues:

What course of action should the appellant follow where the increase in shareholding is pursuant to buy back by the Target Company and there is no active acquisition by the appellants?

Decision:

SAT stated that the appellants would have made an application for exemption from the applicability of provision of Regulation 11 of SEBI (SAST) Regulations, 1997. SAT dispose of the appeal with a direction to the Board to consider the appellant's application for exemption in accordance with law without being influenced by any observation or finding recorded in the impugned order.

IAG Company Limited case⁴⁰

Facts:

On examination of the draft letter of offer filed by Anjaniputra Ispat Limited (Acquirer) for the acquisition of 20% of the issued and paid up capital of IAG Company Limited (Target Company), SEBI observed that the Acquirer has acquired 26,89,592 equity shares representing 41.77% of the current paid up and voting capital of the Target Company over a period of 8 months during the financial years 2008-09 and 2009-10. The increase in the shareholding is made in the following manner:

- a. The Acquirer has acquired 17,19,692 shares (27.64%) on November 19, 2008, thereby, increasing its shareholding from 4.71% to 32.35% of the paid up capital of the Target Company.

⁴⁰ Order of SEBI, WTM/KMA/CFD/303/10/2010.

b. The Acquirer further consolidated its holdings from 32.35% to 41.77% by purchasing 6,06,600 shares (9.42%) i.e. 4.71% each on December 19, 2008 and April 3, 2009.

Issue:

Whether the Acquirer has violated the provisions of Regulation 7(1), 10, 11(1) and 12 of the SEBI (SAST) Regulations, 1997?

Decision:

The acquirer has first triggered the SEBI (SAST) Regulations, 1997 on November 19, 2008 when it had acquired 27.64% shares in the Target Company. However, it has not complied with the provisions of regulation 10 read with regulation 14 of SEBI (SAST) Regulations, 1997 instead it continued to consolidate its shareholding in the Target Company. Further, the manner of acquisition of 4.71% each during two financial years would lead to an inference that the acquirer was well aware of the creeping acquisition limits as specified under regulation 11(1) as otherwise it would have acquired the entire stake in one trench. SEBI ordered that the Adjudicating proceedings should be initiated against the Acquirer under the provisions of SEBI Act, 1992 for the violation of Regulation 10, 11(1) and 12 of the SEBI (SAST) Regulations, 1997.

CONCLUSION

Ensuring certainty and uniformity, while adhering to the principle of equity, can be alleged as the legislative essay if we roll back to the Takeover jurisprudence in India. SEBI regulations, numerous amendments, committee reports, case laws are the evidence of this endeavor. The constitution of TRAC was another land mark set about in this regard. Though the TRAC was constituted to review the current regulations in light of global best practices, to ensure equitable and transparent operation of the market for corporate control and balance the interests of acquirers, investors and target companies, the committee ended up drafting a new set of regulations, which is not just to ‘overturn’ but is an “overtake” of the code.

The committee has recommended increasing the initial trigger from 15% to 25%.⁴¹ It will enable some shareholders like institutional investors to increase their stakes without making an all out tender offer. Secondly, there is an obligation to make disclosures if the acquisition is beyond the thresholds limit i.e. 5%, 10%, 14%, 54%, and 74%. The recommendations require that disclosures be made at 5%, and for every acquisition of 2% or more thereafter, i.e. potentially 10 warnings before the 25% trigger is crossed⁴² therefore making the warnings more rampant. Thirdly, the proposal to make an open offer for acquiring all the shares of the target company⁴³ held by other shareholders will create financial constraints on the acquirers. Fourthly, the report proposed to give discretion to SEBI to decide which case to forward to Takeover Panel for their approval.⁴⁴ In order to maintain uniformity in the decision making process, it would be proper to continue with the existing procedure of referring all cases to the Takeover Panel.

Moreover, before accepting the proposed regulation, it is *sine qua non* to harmonize other SEBI regulations⁴⁵ as opined by experts in this regard. There are a lot of negative and logical reactions to the report, both from the intellectual and industrial world. So, taking care of those responses and amending the new code to the extent to meet the practicalities of the situation will be a noteworthy stride in the evolution of takeover laws.

⁴¹ Supra note 12.

⁴² Supra note 32.

⁴³ Supra note 22.

⁴⁴ Supra note 23.

⁴⁵ SEBI (Delisting of Equity Shares) Regulations 2009, SEBI (ESOS and ESPS) Guidelines, 1999 and others.