

M&A Hotline

November 07, 2008

AMENDMENTS TO TAKEOVER CODE - OVERSIGHT OR INTENDED?

This is further to our most recent hotline "*Creep up to 75% - Takeover Code Relaxed*" discussing the proposed amendments relating to shareholding consolidation under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (the "**Takeover Code**") as announced by the Securities and Exchange Board of India ("**SEBI**") in its press release No. 239/2008 dated October 27, 2008 ("**Press Release**").

Whilst SEBI has finally effected the amendments on this Monday, November 3, 2008 and amended the Takeover Code, the amendments, on several counts, do not correspond to the amendments as suggested by the Press Release.

This Hotline attempts to bring out and discuss the discrepancies between the Press Release and the amendments (as effected), possible reasons behind the discrepancies and finally the implications of the amendments in their current form.

The Discrepancies - Amendments v. Press Release

SEBI has amended Regulation 11(2) of the Takeover Code by inclusion of a proviso, which is summarized as under (the "**Amendments**") —

Any person who holds 55% or more but less than 75% may acquire additional shares or voting rights entitling him up to 5% voting rights in the target company ("Target") if—

- (a) the acquisition is through open market purchase in normal segment on the stock exchange but not through bulk deal /block deal/ negotiated deal/ preferential allotment; or (b) the increase in the shareholding or voting rights of the acquirer is pursuant to a buyback of shares by the Target; and*
- the post acquisition shareholding of the acquirer together with persons acting in concert with him does not increase beyond seventy five per cent (75%).*

A comparison of the Press release with the Amendments is as follows —

| Subject | Press Release | Amendments |
|---|--|--|
| Acquisition of Shares up to 5% | Any person holding 55% or more (but less than 75%) shares of the Target permitted to further increase his shareholding by not more than 5% in the Target without making a public announcement. | Same as the Press Release |
| Increase in shareholding due to buyback | If the shareholding of a shareholder increases up to 5% per annum due to a buyback, then such shareholder will be exempt from making a public announcement. | Public announcement not required if the shareholding of any shareholder holding 55% or more is increased up to 5% due to buyback. No "per annum" time limit stipulated |
| 75% threshold | Not mentioned | Acquirer restricted from increasing his shareholding more than 75% without making a public announcement |

Discrepancies - Reasons and implications

The Amendments appear to be open ended and create ambiguities leaving significant scope for interpretation. Herein below we analyze and attempt to understand SEBI's rationale behind each of these amendments.

ACQUISITION OF SHARES UP TO 5%

One of the most important and critical feature of the Amendments is to do away with the requirement of making a public announcement when a shareholder/acquirer holding 55% or more shares proposes to consolidate his shareholding by further acquisition of up to 5% shares of the Target. Amendments leave it open ended for anyone to interpret whether the 5% acquisition limit stipulated in Regulation 11(2) is applicable to each financial year, or is only a one time affair. In fact, on account of the above ambiguity, though a little far-fetched, it is possible to interpret Regulation 11(2) to imply that a person holding more than 55% shares can go on acquiring shares of the Target from the open market in less than 5% tranches multiple times in a year. However, in light of the spirit of the Takeover Code and more particularly Regulation 11(1), it appears likely that the SEBI intended to apply such 5% limit each financial year.

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Having said that, there are views that SEBI probably wants to permit such creeping acquisitions beyond 55% only once in the lifetime of the Target, and any further acquisitions whether in the same year or in the subsequent years should mandate a public announcement. This view is not entirely without foundation as the Amendments were introduced as an aggressive measure to bolster the bearish stock market, and knowing that SEBI would like to retrogress to a more cautious approach position as and when the markets gain momentum. In fact, earlier this year the Finance Ministry was contemplating steps to make 25% minimum public shareholding a uniformity across the board for listed companies, but decided against it apprehending it might encourage further selling activity from promoters and disappoint an already distressed stock market.

BUYBACK TRIGGERING PUBLIC ANNOUNCEMENT

Another aspect of the Amendments which has come under debate is the application of Regulation 11(2) even to non promoters due to buyback. Amendments mark a significant turning point as shareholders holding 55% or more shares no longer need to approach the takeover panel for seeking exemption from making public announcements for up to 5% increase in their shareholding due to buy back. Prior to the Amendments, shareholders approached the takeover panel under Regulation 4(2) of the Takeover Code to seek exemption from making a public announcement if they anticipated that increase in their shareholding will require a public announcement to be made.

Separately, there are views that the Amendments may be disadvantageous to promoters if their shareholding increases by more than 5% due to an open market buyback, as they will still have to make a public announcement even when they are prohibited from participating in such buybacks.

75% THRESHOLD

The clarification in the Amendments restricting shareholding consolidation beyond 75% leaves a room for interpretation whether the 75% threshold will stand modified to 90% in case of companies which are required to have a minimum public shareholding of 10%. In fact, had the Amendments not stipulated the 75% limit, it would have been only natural to read the 75% threshold in conjunction with the earlier proviso to Regulation 11(2), which provides that the 75% threshold will stand modified to 90% in cases where the listing norms permit minimum public shareholding of 10%.

CONCLUSION

While it remains to be seen whether the discrepancies mentioned above were the result of an oversight by the SEBI or were actually intentional, SEBI should take immediate steps to allay the ambiguities highlighted above to help the acquirers and stakeholders interpret the Amendments in the manner in which they were intended to by the SEBI.

- **Ruchir Sinha & Nishchal Joshipura**

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