M&A Hotline

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SUPREME COURT REVERSES SAT RULING ON DAIICHI'S OPEN OFFER FOR ZENOTECH

Daiichi Sankyo Company Limited ("**Daiichi**"), the Japanese pharmaceutical giant has been haunted by controversies ever since it acquired a controlling stake in Ranbaxy Laboratories Limited ("**Ranbaxy**") on June 11, 2008. Finally, the Supreme Court of India ("**Court**") has come to its rescue through the judgment dated July 08, 2010 which is expected to put to rest all the related controversies. Upholding the claims of Daiichi, the Court has overturned the ruling of the Securities Appellate Tribunal ("**SAT**") dated October 7, 2009 and directed Daiichi to pay to the shareholders of Zenotech Laboratories Limited ("**Zenotech**") an exit price of INR 113.62 per share in the open offer instead of INR 160 per share as directed by SAT.

BACKGROUND

Acquisition of stake in Zenotech by Ranbaxy

Sr. No.	Date	Details	
1.	October 3, 2007	Ranbaxy increased stake in Zenotech through an SPA at INR 160 per share	7% to 45%-triggered open offer under SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 1997 ("**Takeover Code**")
2.	October 5, 2007	Public Announcement of open offer	Reg. 10 and 12 of the Takeover Code
3.	December 24, 2007	Open offer opened	Exit price offered: **INR 160** per share
4.	January 15, 2008	Open offer closed	Ranbaxy acquired 2.2% shares in the open offer

Acquisition of controlling stake in Ranbaxy by Daiichi

Sr. No.	Date	Details	
1.	June 11, 2008	Daiichi acquired controlling stake in Ranbaxy at INR 737 per share	42% through a share purchase and share subscription agreement with the promoters
2.	June 16, 2008	Public Announcement of open offer	Reg. 10 and 12 of Takeover Code
3.	**October 20, 2008**	Daiichi concluded the open offer	Exit price offered: INR 737 per share. Daiichi's total stake in Ranbaxy: 52.5%

Indirect acquisition of stake in Zenotech by Daiichi

Sr. No.	Date	Details	
1.	January 19, 2009	Public Announcement of open offer	Reg. 10 and 12 of Takeover Code. Exit price offered: INR **113.62** per share.
2.	January 27, 2009	Dr. Chigurupati, the promoter of Zenotech challenged the offer price	Detailed representation made to SEBI
3.	June 22, 2009	SEBI Ruling	SEBI decided in favor of Daiichi- Offer price INR 113.62
4.	October 7, 2009	SAT Ruling	SAT overruled the order of SEBI- Offer price INR 160

Objections raised by Zenotech shareholders

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TIMING OF OPEN OFFER

It was claimed that the timing of the open offer for acquisition of shares from the public shareholders of Zenotech is in violation of the Takeover Code. According to them, the open offer for Zenotech should have been made simultaneously with the open offer for Ranbaxy i.e. the offer for Zenotech ought to have been concluded by October 20, 2008.

OPEN OFFER PRICE

It was claimed that the open offer price offered to the shareholders of Zenotech by Daiichi (INR 113.62 per share) is in violation of the Takeover Code. They contended that the offer price should have been INR 160 per share which was the price paid by Ranbaxy to the shareholders of Zenotech in January 2008.

Court's Judgment

TIMING OF OPEN OFFER

The Court has declined to accept the contention of Zenotech's shareholders, and has ruled that the timing of the open offer made by Daiichi is in compliance with the provisions of the Takeover Code. According to Reg. 14(4) of the Takeover Code, the public announcement of an open offer for indirect acquisition could be made by the acquirer within three months of consummation of acquisition or change in control of or restructuring of the parent or the holding company. The public announcement of open offer for Zenotech shareholders was made by Daiichi on January 19, 2009 which is clearly within three months from October 20, 2008, the date of completion of acquisition of Ranbaxy by Daiichi.

OPEN OFFER PRICE

Open offer price is calculated under Reg. 20(4) of the Takeover Code, which prescribes three different modes of calculation including the *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.*

In case of an indirect acquisition, the mechanism for determining the offer price is prescribed by Reg. 20(12) which states that the exit price should be calculated under Reg. 20(4) with two different reference dates; (i) the date of public announcement for the parent (June 16, 2008) and (ii) the date of public announcement for the target (January 19, 2009). Ultimately, that price will be fixed which is highest of all the prices under Reg. 20(4).

Since there was no existing negotiated price (Reg. 20(4)(a)) and Daiichi had not purchased the shares of Zenotech in the previous 26 weeks (Reg. 20(4)(b)), it was argued by Daiichi that only Reg. 20(4)(c) would apply. Therefore the offer price was fixed at INR 113.62, being 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. This price was not acceptable to Zenotech's shareholders who argued that the price should have been INR 160 per share under Reg. 20(4)(b). It was argued that Reg. 20(4)(b) covers not only acquisition by the acquirer, but also by the persons acting in concert ("**PAC**") with the acquirer. They contended that Ranbaxy is a PAC of Daiichi and therefore, the price paid by Ranbaxy to the shareholders of Zenotech in January 2008 is relevant for determining the exit price offered by Daiichi to Zenotech's shareholders under Reg. 20(4)(b). The Court rejected this contention of Zenotech's shareholders.

WHO IS A PAC?

The critical question to be determined by the Court was whether Ranbaxy and Daiichi are PACs of each other for the purposes of acquisition of Zenotech's shares. The Court answered this question in the negative and clearly established that Ranbaxy and Daiichi were not PACs at the time of acquisition of shares of Zenotech by Ranbaxy, in January 2008. The Court relied on the definition of PAC under Reg. 2(e)(1) of the Takeover Code to show that ***a common objective and purpose to acquire shares or voting rights*** is a mandatory prerequisite to constitute PACs under the Takeover Code. Without such common objective and concerted action as provided under Reg. 2(e)(1), the two alleged parties would never be PACs and this is the fundamental test to determine PACs. 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 or voting rights of a target company, they would not comprise PAC.

ARE DEEMED PACS ALWAYS PACS?

The Court explained that all the deemed PACs identified under Reg. 2(e)(2) are also subject to the test under Reg. 2(e)(1), as provided above. The Takeover Code identifies and enlists certain PACs as deemed PACs which by virtue of their mutual relationship, give rise to a prima facie presumption of acting with a common objective, ***unless the contrary is established***. However, this presumption is not absolute and is rebuttable by the alleged parties, as provided in Reg. 2(e)(2).[1] Further, the deeming provision (Reg. 2(e)(2)) would come into picture, only from the date on which two or more persons come together in one of the specified relationships, and not from any earlier date. Hence, there is no retrospective effect in application of the concept of a deemed PAC.

Reg.2(e)(2)(i) treats a holding company and its subsidiary as deemed PACs, by virtue of their relationship. However, this assumption is subject to requirements of common objective and purpose under Reg. 2(e)(1). Hence, the Court has established that a holding company and its subsidiary may not be PACs, if they do not fulfill the requirement of common objective and purpose to acquire shares or voting rights as provided under Reg. 2(e)(1).

WHO IS A RELEVANT PAC FOR THE PURPOSES OF REG. 20(4)(B)?

The language of Reg. 20(4)(b) clarifies that the relevant PACs for the purposes of the Regulation, are only those persons, who qualify as PACs at the time of the relevant acquisition of the shares of the target. The status of PAC is not a permanent one, and it is a settled position of law, that 'once a PAC' does not mean 'always a PAC'. Reg.20(4)(b) captures only those persons who are PACs of the acquirer, for a specific acquisition, and not every PAC of the acquirer in the past or in the future.

Applying this rationale to the instant case, the Court stated that Ranbaxy as the subsidiary of Daiichi is deemed to be a PAC of Daiichi under the Takeover Code, as of today. However, they did not qualify as PACs under the Takeover Code for the acquisition of shares of Zenotech as Ranbaxy and Daiichi did not have any common object or purpose to acquire the shares or voting rights of the Zenotech when the agreement was executed between Ranbaxy and Daiichi on June

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11, 2008. Acquisition of Zenotech's shares by Daiichi was only consequential to the acquisition of Ranbaxy and not a concerted action. Hence they do not comply with the requirements under Reg. 2(e)(1) to constitute PAC.

Also, what is relevant for the purposes of Reg. 20(4) is that, when Ranbaxy had acquired shares of Zenotech in January 2008, it should have been a PAC of Daiichi on that very date and not on any other date. Ranbaxy became the subsidiary of Daiichi only on October 20, 2008 and prior to that, there was no relationship, whatsoever, between Ranbaxy and Daiichi.

CONCLUSION

The Court, through this judgment has brought about much required clarity on the provisions of the Takeover Code relating to PACs. To this end, the Court has relied extensively on the reports of Justice P. N. Bhagwati Committee, 1997 and the Reconvened Committee on Takeover Code, 2002 (under the chairmanship of Justice P. N. Bhagwati), to analyse the provisions of the Takeover Code. Acknowledging the help and assistance provided by these committee reports, the Court has highlighted the significance of 'object and purpose' clause in interpreting statutes. Further, it has been asserted by the Court that as in the case of Acts, it is necessary to include 'object and purpose' clause in subordinate legislations like Regulations to make their interpretation by the Court, more effective, easier and in line with object of their enactment. In this regard, the Court has called for a change in the legislative policy to introduce 'object and purpose' clause in all delegated legislations, bearing in mind the fact that highly complex and specialized spheres of activities are being regulated by subordinate legislations.

- Arun Scaria & Nishchal Joshipura

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1 Reg. 2(e)(2): "W*ithout prejudice to the generality of this definition, the following persons will be deemed to be persons acting in concert with other persons in the same category,* ***unless the contrary is established***"

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