



M&A LAB

CAIRN - VEDANTA

Deal Dissection

Dissected by Team M&A and Team Globalisation:

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CONTENTS

I.	PROLOGUE	1
II.	PARTIES INVOLVED IN THE DEAL	1
III.	DEAL SNAPSHOT	4
IV.	CHRONOLOGY OF KEY EVENTS	7
V.	DEAL SUMMMARY	13
1.	How was the acquisition consummated and what were the terms of the Agreement dated August 15, 2010?	13
2.	Amendment date April 21, 2011: What changed?	15
3.	What were the changes made to the Agreement?	16
VI.	COMMERCIAL CONSIDERATIONS	16
1.	Why did Vedanta group choose to enter oil and gas sector?	16
2.	Why did Vedanta group target Cairn India?	17
3.	What strategic benefits does Cairn UK Parent seek to reap from the Deal?	18
4.	How is the Deal financed?	20
5.	How did the Deal affect the prices of the shares of various corporate stakeholders?	21
6.	Did the minority shareholders of Cairn India have any concerns arising from the Deal?	23
VII.	LEGAL AND REGULATORY CONSIDERATIONS	24
1.	How does the Indian government and ONGC get to interfere in the Deal?	24
2.	Why was the matter referred to Cabinet Committee on Economic Affairs for their approval?	25
3.	What was the dispute on the conditions relating to royalty and cess arbitration imposed for the grant of approval to the Deal?	26
4.	Why were put option and call option arrangements removed from the Deal documents?	28
5.	Why did Vedanta group agree to buy 10% share capital of Cairn India prior to government approval under the revised arrangement?	29
6.	Can an amendment agreement trigger the combination provisions of the Competition Act?	30
7.	Why was RBI approval required for the Deal?	31
8.	Why did Vedanta make an Open Offer under the Takeover Code, 1997?	32
9.	Can an acquirer acquire shares of the target company during the open offer period?	33

10.	What impact could the new Takeover Code, 2011 have on the Deal?	33
11.	Why was the approval of the shareholders of Sesa Goa and Sesa Resources required to consummate the Open Offer pursuant to Section 372A of the Act?	34
12.	What are the corporate governance issues with respect to the interests of the minority shareholders against the backdrop of Deal?	35
13.	Do the actions of government violate India's obligations under Bilateral Investment Treaty with United Kingdom?	35
14.	Was the non-compete fee justifiable in the facts of the Deal?	35
15.	Did the Deal trigger any provisions of the Listing Rules of UK Listing Authority for Vedanta Resources and Cairn UK Parent?	36
VIII.	TAX CONSIDERATIONS	37
1.	What are the tax implications of the sale of shares of Cairn India by Cairn UK Sub in India?	37
2.	What are the tax implications of the sale of shares of Cairn India by Cairn UK Sub in UK?	38
3.	What are the tax implications of the sale of shares of Cairn India by Petronas in India?	39
IX.	EPILOGUE	39
X.	CONCLUDING REMARKS	40

I. PROLOGUE

A roller coaster ride that began close to 16 (sixteen) months ago came to a halt when the much protracted deal recently consummated whereby UK based Vedanta group acquired a controlling stake in Cairn India Limited (the “Deal”). With a long haul for this acquisition, Mr. Anil Agarwal, chairman of the London listed Vedanta Resources PLC, made an optimistic remark that “*It is definitely a little late, but (as they say) der aaye durust aaye (better late than never)*”¹. The long stop date for completion of the Deal was revised more than once, and was finally set as December 15, 2011 by the parties in July, 2011.²

The Deal that withstood the test of time and sailed through the dark waters of regulatory uncertainty has closed recently. This Deal has earmarked a beginning of a new era in the Indian oil industry; which led Mr. Jaipal Reddy, Minister of Petroleum and Natural Gas, Union of India, to assert while addressing the World Petroleum Congress on December 5, 2011 that: “*two major investment decisions made by major companies BP (British Petroleum) and Vedanta ... have re-established faith in the hydrocarbon potential in India*”³.

In this M&A Lab, we seek to streamline the legal and commercial undercurrents that characterize the acquisition of approximately 59% of voting capital in Cairn India Limited by the Vedanta Resources PLC and its group companies.

The Deal was shaken by the multipronged intervention by the Government of India and concluded after a series of dramatic events, involving both private players and public authorities. Our attempt is to read and interpret the signals of regulators, market and parties to the Deal, and to analyze the commercial, legal, regulatory and tax implications of the Deal. This M&A Lab also intends to provide an insight into what this instance of regulatory intervention holds for the stakeholders of the Deal.

As the Deal is characterized by peculiar legal connotations, this M&A Lab will separately deal with the commercial aspects and regulatory ramifications, though both aspects have influenced each other.

II. PARTIES INVOLVED IN THE DEAL

1. TARGET COMPANY

Cairn India Limited (“**Cairn India**”) was incorporated as a public limited company on August 21, 2006 under the (Indian) Companies Act, 1956 (“**Act**”) and promoted by Cairn UK Holdings Limited, a wholly owned subsidiary of Cairn Energy PLC. Cairn India is engaged in the business of crude oil and natural gas exploration and production. It operates the largest producing oil field in the Indian private sector and has pioneered the use of cutting-edge technology to extend production life. It holds

¹Q&A: Anil Agarwal, Vedanta Resources; <http://www.sify.com/finance/q-a-anil-agarwal-vedanta-resources-news-equity-lmjibveijfag.html>, last visited on December 24, 2011.

²

[http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20\(Jan%202012\).pdf](http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20(Jan%202012).pdf); last visited on January 14, 2012

³http://articles.economictimes.indiatimes.com/2011-12-05/news/30477754_1_cairn-vedanta-deal-cairn-operated-bp-reliance; last visited on December 28, 2011

material exploration and production positions in 11 blocks in west and east India along with new exploration rights elsewhere in India and Sri Lanka. The equity shares of Cairn India have been listed on the Bombay Stock Exchange (“**BSE**”) and the National Stock Exchange (“**NSE**”) since January 9, 2007.⁴

2. SELLER GROUP

(i) Cairn Energy PLC

Cairn Energy PLC (“**Cairn UK Parent**”) was incorporated in 1981 in Scotland.⁵ Headquartered in Edinburgh, it is a global oil and gas exploration company. Over the last 20 years, Cairn UK Parent has concentrated its activities in South Asia, with operations in India, Bangladesh and Nepal. It also has operations in Spain and Greenland.⁶ On December 22, 1988, it was listed on the London Stock Exchange (“**LSE**”).⁷

(ii) Cairn UK Holdings Limited

Cairn UK Holdings Limited (“**Cairn UK Sub**”) was incorporated on June 26, 2006 and has its registered office in Edinburgh.⁸ It is a wholly owned subsidiary of Cairn UK Parent and is the holding company of Cairn India.

Cairn UK Parent and Cairn UK Sub will be together hereinafter referred to as the “**Seller Group**” hereafter.

3. ACQUIRER GROUP

(i) Vedanta Resources PLC

Vedanta Resources PLC (“**Vedanta Resources**”) was incorporated as a private company limited by shares by the name of ‘Angelchange Limited’ on April 22, 2003 in UK. The name of the company was changed to ‘Vedanta Resources Limited’ on June 26, 2003. The company was re-registered as a public limited company on November 20, 2003 under the name ‘Vedanta Resources PLC’. Vedanta Resources is the flagship company of the Vedanta group, a diversified industrial group based out of UK with interests in metals and mining and operations spanning the globe with significant interests in India. The promoter of Vedanta Resources is Volcan Investments Limited owned by a family trust of Mr. Anil Agarwal. The shares of Vedanta Resources are listed on the LSE.⁹

⁴ http://www.bseindia.com/xml-data/corpfilings/AttachHis/Cairn_India_Ltd_180810.pdf, last visited on December 26, 2011

⁵ <http://shareholdersportal.co.uk/ftse-stocks/cairn-energy-plc> last visited on December 27, 2011; [http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20\(Jan%202012\).pdf](http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20(Jan%202012).pdf); last visited on January 14, 2012

⁶ <http://www.cairnenergy.com/about-cairn/> last visited on December 27, 2011

⁷ <http://www.londonstockexchange.com/exchange/prices-and-markets/stocks/summary/company-summary.html?fourWayKey=GB00B59MW615GBGBXSET1>, last visited on December 27, 2011

⁸ <http://www.cdrex.com/cairn-uk-holdings-limited-1130143.html> last visited on December 27, 2011

⁹ http://www.bseindia.com/xml-data/corpfilings/AttachHis/Cairn_India_Ltd_180810.pdf, last visited on December 26, 2011

(ii) Twin Star Energy Holdings Limited

Twin Star Energy Holdings Limited (“**Twin Star**”) is a limited company originally incorporated as ‘Arlington Investment Limited’ on February 27, 2008 with its registered office in St. Port Louis, Mauritius. Its name was changed to ‘THL Aluminium Limited’ with effect from May 9, 2008, and subsequently to ‘Twin Star Energy Holdings Limited’ with effect from August 19, 2010. Twin Star is part of the Vedanta group and is an indirect wholly owned subsidiary of Vedanta Resources.¹⁰

(iii) Sesa Goa Limited

Sesa Goa Limited (“**Sesa Goa**”) was incorporated as a private limited company on June 25, 1965 under the Act. Sesa Goa became a public limited company pursuant to its initial public offer in the year 1981. It became a subsidiary of Vedanta Resources pursuant to acquisition of controlling stake in Sesa Goa by the latter. Sesa Goa, one of India’s largest producers and exporters of iron-ore in the private sector, is engaged in the business of exploration, mining and processing of iron-ore. Its mining operations are carried out in the states of Goa, Karnataka and Orissa in India. The company has also diversified its operations into manufacturing of pig iron and metallurgical coke. The shares of Sesa Goa are listed on the BSE and the NSE.¹¹

(iv) Sesa Resources Limited

Sesa Resources Limited (“**Sesa Resources**”) (formerly known as V.S. Dempo and Co. Private Limited) was incorporated as a private limited company on April 22, 1965 under the Act. 100% of the share capital of the company was acquired by Sesa Goa in June 2009. Sesa Resources is engaged in the business of mining iron-ore in the state of Goa.¹²

Vedanta Resources, Twin Star, Sesa Goa and Sesa Resources will be collectively referred to as the “**Acquirer Group**” hereinafter.

4. OTHERS

(i) Petronas International Corporation Limited

Petronas International Corporation Limited (“**Petronas**”) is a wholly-owned subsidiary of Petroliam Nasional Berhad. Incorporated on January 24, 1998, Petronas is an investment holding company based out of Labuan, Malaysia and is in the business of finance.¹³

¹⁰ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_180810.pdf, and <http://www.sebi.gov.in/takeover/cairnlof.pdf>, last visited on December 26, 2011

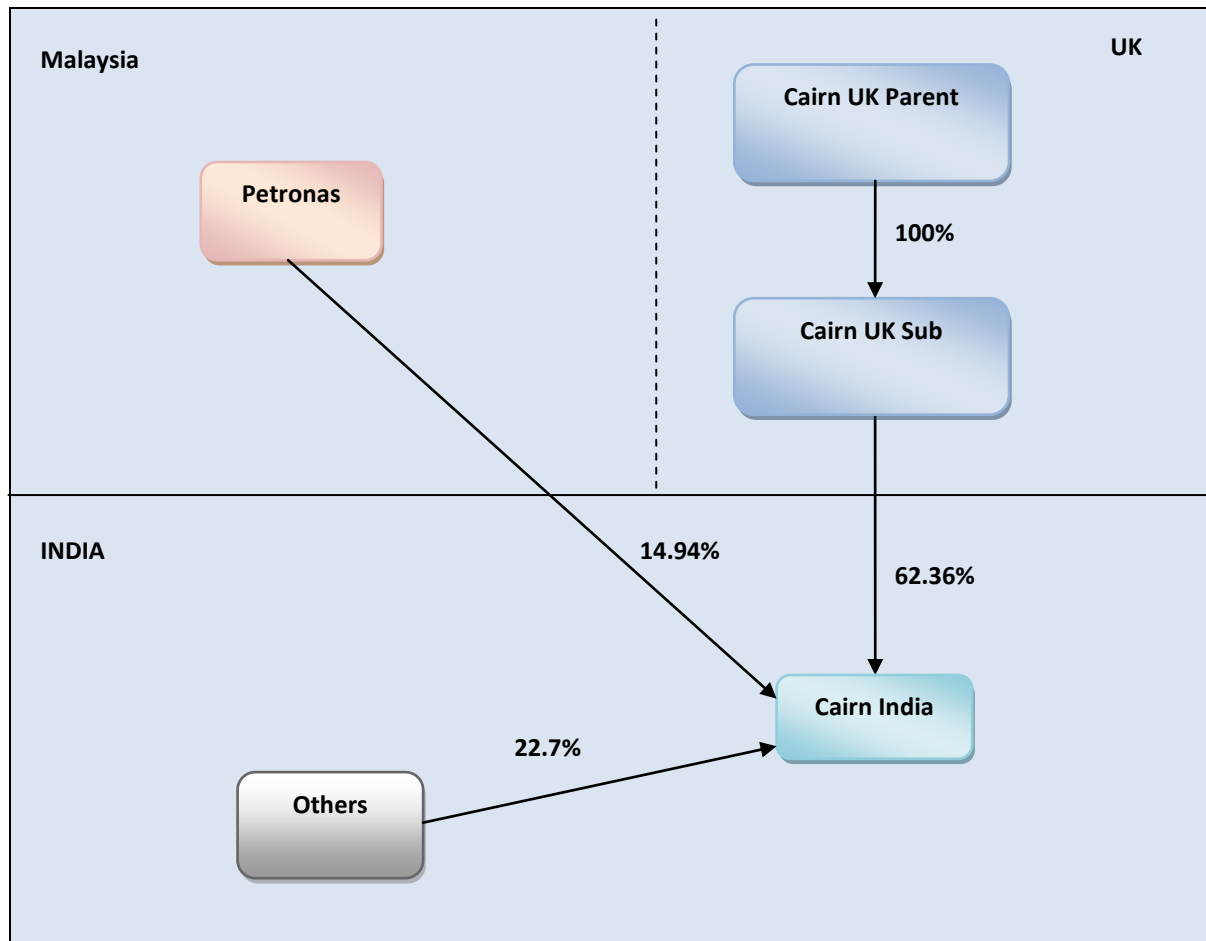
¹¹ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_180810.pdf, last visited on December 26, 2011

¹² <http://www.sebi.gov.in/takeover/cairnindiakorrigien.pdf>, last visited on December, 27, 2011

¹³ http://www.petronas.com.my/about_us/directory/petronas_directory.aspx?CompanyId=3975, last visited on December 27, 2011

III. DEAL SNAPSHOT

1. SHAREHOLDING PATTERN OF CAIRN INDIA PRIOR TO THE DEAL¹⁴



2. DEAL SNAPSHOT

Acquirer Group	Vedanta Resources, Twin Star, Sesa Goa and Sesa Resources ¹⁵
Sellers	Cairn UK Sub, Petronas and public shareholders of Cairn India. ¹⁶
Voting Capital	“ Voting Capital ” shall mean the total equity share capital and voting rights of Cairn India, on a fully diluted basis as on the date of consummation of the sale and purchase under the Agreement (“ Closing Date ”). As per the disclosures made to the BSE by Cairn UK Sub on December 8, 2011 ¹⁷ under the Takeover Code, 2011, the total fully diluted share / voting capital of Cairn India is 1,923,727,589

¹⁴ Shareholding pattern as disclosed to the stock exchanges for the quarter ending September, 2010; available at http://www.bseindia.com/shareholding/shareholdingPattern_60.asp?scripcd=532792&qtrid=67.00, last visited on February 27, 2012

¹⁵ <http://www.bseindia.com/stockinfo/anndet.aspx?newsid=daea373d-d8e5-49ff-987a-11be1e25d27a¶m1=1>, last visited on December 28, 2011

¹⁶ *Ibid*

¹⁷ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_081211_SAST.pdf

<p>Total acquisition</p>	<p>equity shares.</p> <p>Total: 1,122,713,999 shares representing 58.361% of the Voting Capital of Cairn India.¹⁸</p> <p>April 19, 2011</p> <p>I. From Petronas to Sesa Goa as a bulk deal:</p> <p>200,000,000 equity shares of Cairn India, representing 10.396% of the Voting Capital, at price of INR 331 per share.¹⁹</p> <p>Open Offer (Open Offer period April 11 – April 30)</p> <p>II. Through an open offer (“Open Offer”) under SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 1997 (“Takeover Code, 1997”), by Sesa Goa:</p> <p>155,033,172 equity shares of Cairn India, representing 8.058% of the Voting Capital²⁰, at a price of INR 355.²¹</p> <p>Post Open Offer</p> <p>III. Pursuant to Share Purchase Agreement dated August 15, 2010 (“Agreement”), <i>inter alia</i> between Vedanta Resources and Cairn UK Parent, amended by an amendment agreement dated June 27, 2011:</p> <p>(a) From Cairn UK Sub and its nominees to Twin Star (off market) (July 11, 2011)</p> <p>191,920,207 equity shares of Cairn India, representing 9.976% of the Voting Capital, at a price of INR 355 per share²²</p> <p>(b) From Cairn UK Sub to Sesa Goa and Sesa Resources as a bulk deal at a price of INR 325 per share (December 7, 2011):²³</p>
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¹⁸ <http://www.bseindia.com/stockinfo/anndet.aspx?newsid=1c84fd94-23de-43f2-aed4-e79d385726ff¶m1=1>, last visited on December 28, 2011

¹⁹ Form A, filed by Cairn India, April 21, 2011, under SEBI (Prohibition of Insider Trading), 1992; <http://www.bseindia.com/stockinfo/anndet.aspx?newsid=1ddfbc29-df23-4048-9b5b-424d33decd71¶m1=1>, last visited on December 28, 2011

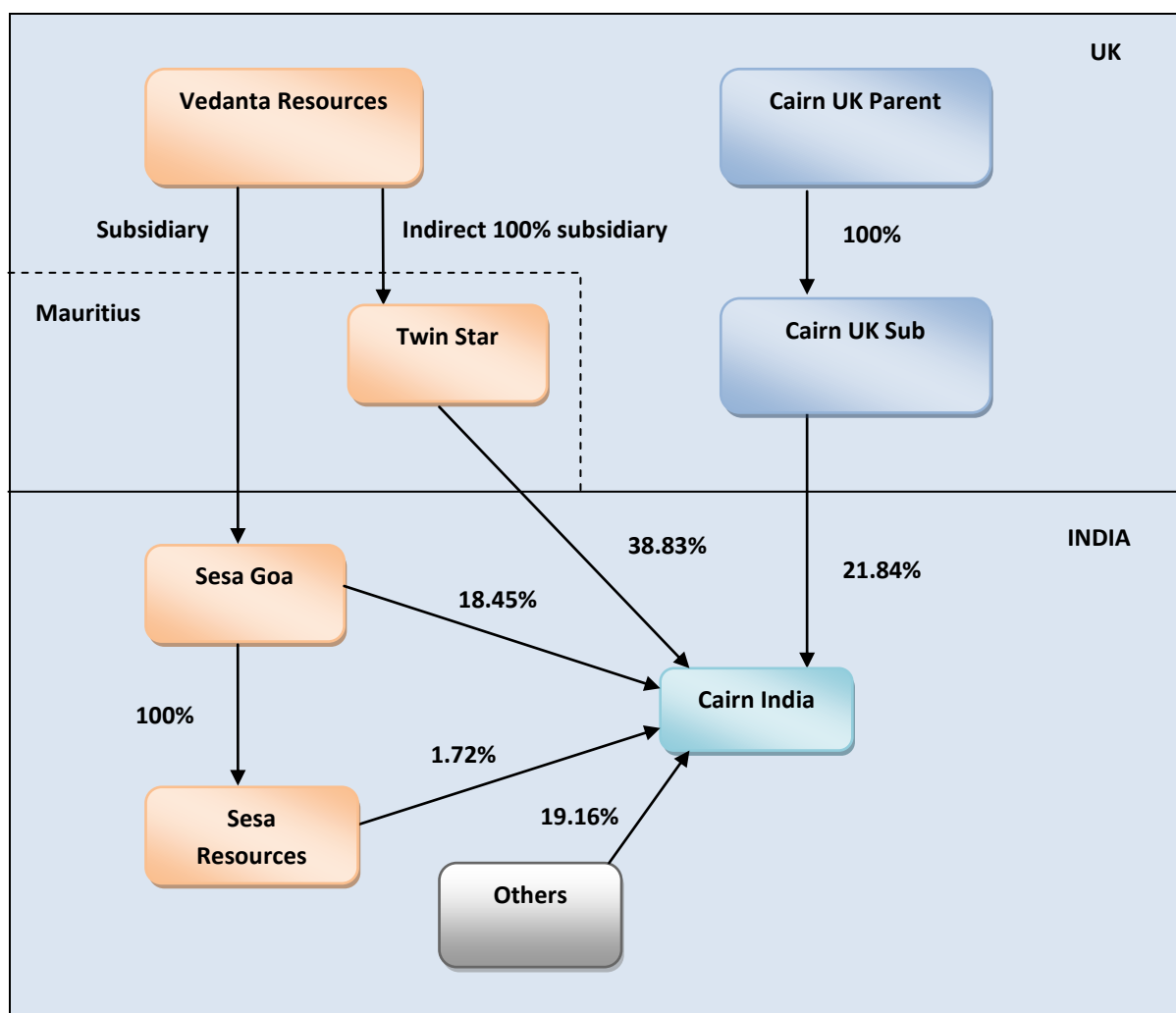
²⁰ Notice of postal ballot, http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_080811.pdf, last visited on December 28, 2011

²¹ Public Announcement; <http://www.sebi.gov.in/takeover/public/cairnpa.pdf>, last visited on December 28, 2011

²² http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd1_130711_SAST.pdf; last visited on December 27, 2011

	<p>28,807,241 shares representing 1.497% of the Voting Capital;</p> <p>(c) From Cairn UK Sub to Twin Star (off-market) (December 8, 2011):</p> <p>546,953,379 shares representing 28.431% of the Voting Capital, at a price of INR 355 per share.²⁴</p>
Total Consideration	INR 392.899 billion (approximately USD 7.857 billion ²⁵) for acquisition of 58.361% of shares in Cairn India.

3. SHAREHOLDING PATTERN OF CAIRN INDIA POST THE DEAL²⁶



²³ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_091211_SAST1.pdf; last visited on December 27, 2011

²⁴ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_091211_SAST1.pdf; last visited on December 27, 2011.

²⁵ Assuming 1 USD = INR 50

²⁶ Shareholding pattern as disclosed to the stock exchanges for the quarter ending December, 2011; available at http://www.bseindia.com/shareholding/shareholdingPattern_60.asp?scripcd=532792&qtrid=72.00, last visited on February 27, 2012

IV. CHRONOLOGY OF KEY EVENTS

DATE	KEY EVENT
August 15, 2010	<p>The Acquirer Group and the Seller Group entered into an Agreement, pursuant to which the Acquirer Group agreed to acquire from Cairn UK Sub (either by itself or through any person nominated by it, including Sesa Goa) such number of equity shares representing at least 51% of the Voting Capital, as reduced by (a) and (b) below ("Sale Shares"): </p> <p>(a) the number of equity shares validly tendered in the open offer up to a maximum of 11% of the Voting Capital, provided that the Sale Shares shall in no event be reduced below 40% of the Voting Capital pursuant to the adjustment under this (a); and²⁷</p> <p>(b) any transfer of equity shares by the Seller Group (other than the Sale Shares) for emergency funding reasons following severe financial difficulty prior to consummation of the sale and purchase of the Sale Shares in terms of the Agreement.</p> <p>Provided that the aggregate of equity shares to be acquired pursuant to the open offer and the Agreement shall not be less than 51% of the Voting Capital.²⁸</p>
August 16, 2010	<p>Sesa Goa informed BSE regarding a press release titled "<i>Sesa Goa Limited (Sesa Goa) to acquire a 20% Strategic Investment in Cairn India Ltd ('Cairn India') (The Proposed Investment)</i>".²⁹</p> <p><u>Transaction highlights</u></p> <p>Sesa Goa to acquire approximately 20% of the issued share capital of Cairn India under an open offer for a consideration of approximately USD 3 billion. If there is insufficient take up in the open offer, Sesa Goa will acquire the balance as part of the Acquirer Group's acquisition of a 51%-60% stake in Cairn India. Sesa Goa will fund the proposed investment primarily through its cash balances.</p>
August 17, 2010	<p>JM Financial Consultants Private Limited ("Manager to the Offer"), on behalf of Twin Star and Vedanta Resources ("Acquirers") along with Sesa Goa Limited (being a person acting in concert with the Acquirers ("PAC")), issued a public announcement ("PA") to the equity shareholders of Cairn India pursuant to and in compliance with, Regulation 10 and Regulation 12 and other applicable provisions of the Takeovers Regulations, 1997.³⁰</p>

²⁷ At the time of Agreement, 51% of Voting Capital represented 979,162,688 equity shares and 41% of Voting Capital represented 767,970,736 equity shares.

²⁸ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_180810.pdf, last visited on December 26, 2011

²⁹ <http://www.bseindia.com/gresann/newsh.asp?newsid={BCFA872D-E445-4A8A-952B-8FAF3A91E166}¶m1=1>, last visited on December 27, 2011

³⁰ <http://www.bseindia.com/gresann/news.asp?newsid={B7372A10-C287-42E7-986A-9F48445AFB36}>, and <http://www.bseindia.com/gresann/news.asp?newsid={C43FE3F6-65CF-47EF-AECF-BB36048D07DE}>, last visited on December 26, 2011

DATE	KEY EVENT
	<p><u>The offer:</u></p> <p>The Acquirers and PAC made the offer (“Open Offer”) to the equity shareholders of Cairn India (other than the parties to the Agreement and any other group companies of Seller Group) to acquire up to an aggregate of 383,985,368 equity shares of face value of INR 10 each of Cairn India constituting 20% of the fully diluted voting capital of Cairn India as at fifteen days post the closure of the Open Offer at a price of INR 355 per share, in accordance with the Takeovers Regulations, 1997 and subject to the terms and conditions mentioned in the PA and in the letter of offer (“Letter of Offer”).</p> <p><u>Schedule of Activities:</u></p> <p>Specified Date - August 20, 2010 Date of Opening of the Open Offer - October 11, 2010 Date of Closing of the Open Offer - October 30, 2010</p>
August 31, 2010	The Government of India requested Cairn UK Parent to seek approval for its proposed sale of majority shareholding in Cairn India in respect of various Production Sharing Contracts (“ PSCs ”) ³¹ to which Cairn India and its subsidiaries (“ CIG ”) are a signatory. ³² CIG, after initial protest, later acceded to the request and made a formal application to the Government of India.
October 7, 2010	The resolution proposed at the general meeting of Cairn UK Parent on the proposed sale by its wholly-owned subsidiary, Cairn UK Sub, of a maximum of 51% of the Voting Capital of Cairn India on the terms and subject to the conditions set out in the Agreement was approved. ³³
October 15, 2010	The shareholders of Sesa Resources granted the required approval under section 372A of the Act for the acquisition of shares of Cairn India under the Open Offer. ³⁴
October 18, 2010	The shareholders of Sesa Goa granted the required approval under section 372A of the Act for the acquisition of shares of Cairn Indian under the Open Offer. ³⁵
December 10, 2010	The resolution proposed at the general meeting of Vedanta Resources on the proposed sale by Cairn UK Sub, of a maximum of 51% of the Voting Capital of Cairn India on the terms and subject to the conditions set out in the Agreement was approved. ³⁶

³¹ New Exploration and Licensing Policy (NELP) blocks viz. PR-OSN-2004/1, MB-DWN-2009/1, KG-OSN-2009/3, KG-ONN-2003/1, KG-DWN-98/2, GS-OSN-2003/1 and KK-DWN 2004/1 and Pre-NELP blocks, viz. RJ-ON-90/1, Ravva (PKMG-1) and CB-OS/2)

³² http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_080811.pdf, last visited on December 27, 2011

³³ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_081010.pdf, last visited on December 26, 2011

³⁴ <http://www.sebi.gov.in/takeover/cairnlof.pdf>, last visited on December 27, 2011

³⁵ <http://www.sebi.gov.in/takeover/cairnlof.pdf>, last visited on December 27, 2011

³⁶ <http://www.sebi.gov.in/takeover/cairnlof.pdf>, last visited on December 27, 2011

DATE	KEY EVENT														
April 5, 2011	Corrigendum to the PA was issued on behalf of the Acquirers and PAC. As per the corrigendum, Sesa Resources was included as a PAC with the Acquirers along with Sesa Goa. ³⁷														
April 6, 2011	<p>The parties to the Agreement entered into an amendment agreement to the Agreement, whereby it was agreed to extend the long stop date for the completion of all conditions (unless waived otherwise) from April 15, 2011 to May 20, 2011.³⁸</p> <p>Vedanta Resources subsidiary, Sesa Goa announced receipt of clearance from SEBI to send Letter of Offer to shareholders of Cairn India and proceed with the Open Offer of approximately 20% of the shares of Cairn India.³⁹</p>														
April 7, 2011	<p>Sesa Goa posted the Letter of Offer to acquire up to 383,985,368 shares of Cairn India representing 20% of the fully diluted voting capital of Cairn India as at fifteen days post the closure of the Open Offer at a price of INR 355 per share. The Open Offer would open on April 11, 2011 and close on April 30, 2011.⁴⁰</p> <p>Further, the disclosure provided by Vedanta Resources to the LSE on the same date, mentioned that the SEBI had notified to Vedanta Resources that the put and call options as agreed to be exercisable by Cairn UK Parent and Vedanta Resources, respectively, and the pre-emption right as agreed to be exercisable by Vedanta Resources in connection with the Deal, must be removed from the Agreement as they do not comply with Indian securities regulations. As a result of this and to allow the Open Offer to proceed, Cairn UK Parent and Vedanta Resources agreed that the put and call options shall be removed. Vedanta Resources also agreed that its pre-emption right shall be removed.⁴¹</p> <p><i>Timeline for the Open Offer:</i></p> <table border="1"> <thead> <tr> <th>DATE</th> <th>ACTIVITY</th> </tr> </thead> <tbody> <tr> <td>August 17, 2010</td> <td>Public Announcement</td> </tr> <tr> <td>August 20, 2010</td> <td>Specified Date⁴²</td> </tr> <tr> <td>September 7, 2010</td> <td>Last date for a competitive bid</td> </tr> <tr> <td>April 6, 2011</td> <td>Date by which Letter of Offer to be dispatched to Shareholders</td> </tr> <tr> <td>April 11, 2011</td> <td>Date of opening of the Open Offer</td> </tr> <tr> <td>April 19, 2011</td> <td>Last date for upward revision of the Open Offer price /</td> </tr> </tbody> </table>	DATE	ACTIVITY	August 17, 2010	Public Announcement	August 20, 2010	Specified Date ⁴²	September 7, 2010	Last date for a competitive bid	April 6, 2011	Date by which Letter of Offer to be dispatched to Shareholders	April 11, 2011	Date of opening of the Open Offer	April 19, 2011	Last date for upward revision of the Open Offer price /
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³⁷ <http://www.sebi.gov.in/takeover/cairnindiacorrigen.pdf>, last visited on December, 27, 2011

³⁸ <http://www.sebi.gov.in/takeover/cairncorrigen2.pdf>, last visited on December 27, 2011

³⁹ <http://www.londonstockexchange.com/exchange/news/market-news/market-news-detail.html?announcementId=10833787>, and http://www.bseindia.com/xml-data/corpfilling/AttachHis/Sesa_Goa_Ltd_060411.pdf, last visited on December 27, 2011

⁴⁰ http://www.bseindia.com/xml-data/corpfilling/AttachHis/Sesa_Goa_Ltd_070411.pdf. last visited on December 27, 2011

⁴¹ <http://www.londonstockexchange.com/exchange/news/market-news/market-news-detail.html?announcementId=10835084>, last visited on December 27, 2011

⁴² Specified date is only for the purpose of determining the names of the shareholders as on such date to whom the Letter of Offer would be sent. All owners (registered or unregistered) of the equity shares (other than the parties to the Agreement and any other group company of the Seller Group) are eligible to participate in the offer any time before the closing of the Offer.

DATE	KEY EVENT	
		number of Equity Shares
	April 26, 2011	Last date for withdrawing acceptance of the Open Offer
	April 30, 2011	Date of closing of the Open Offer
	May 15, 2011	Last date of communicating rejection / acceptance and payment of consideration for accepted tenders and/or the unaccepted equity shares / share certificates will be dispatched/credited
April 19, 2011	<p>Sesa Goa acquired 200,000,000 equity shares constituting 10.396% of the Voting Capital Cairn India from Petronas at a price of INR 331 by way of bulk deal.⁴³ Petronas had sold 283,431,438 shares constituting 14.733% of the Voting Capital of Cairn India.⁴⁴</p> <p>Sesa Goa submitted to BSE an announcement relating to Open Offer for Cairn India shares, whereby it clarified that the Open Offer was not subject to the Government of India's consent.⁴⁵ The Letter of Offer had indicated that as per the PSCs entered into by Cairn India, the Deal would be subject to the Government of India's consent.</p>	
April 21, 2011	By virtue of the amendment agreement to the Agreement, the parties thereto agreed that the Sale Shares shall be determined as such number of equity shares representing 51% of the Voting Capital as reduced by the number of equity shares validly tendered in the Open Offer <u>and</u> 200 million equity shares acquired at any time prior to the date of consummation of the sale and purchase under the Agreement from any third party outside of the Open Offer.	
May 18, 2011	The post Open Offer public announcement mentioned that out of the proposed offer of 20% of the fully diluted voting capital of Cairn India as at fifteen days post the closure of the Open Offer, only 8.058% of the Voting Capital was acquired under the Open Offer. ⁴⁶ As per this document, post the Open Offer, the shareholding of the Acquirer Group in Cairn India rose from 10.396% (acquired separately after the Public Announcement) to 18.455% of the Voting Capital. ⁴⁷	
June 27, 2011	<p>Cairn UK Parent and Vedanta Resources agreed to certain adjustments to the Agreement for the part sale of shares of Cairn India, as follows:</p> <ul style="list-style-type: none"> (i) removal of non-compete arrangement and associated fee, which are expected to result in a 5.3% reduction in post-tax proceeds; and (ii) the Deal to be consummated in two tranches – an initial sale of 10% stake in Cairn India and a subsequent sale of 30% stake which remains subject to 	

⁴³ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_210411_SAST.pdf, and <http://www.londonstockexchange.com/exchange/news/market-news/market-news-detail.html?announcementId=10845409>; last visited on December 27, 2011

⁴⁴ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_210411_SAST1.pdf, last visited on December 27, 2011

⁴⁵ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Sesa_Goa_Ltd_190411.pdf, last visited on December 27, 2011

⁴⁶ <http://www.sebi.gov.in/takeover/public/cairnpopa.pdf>, last visited on December 27, 2011

⁴⁷ *Id.*

DATE	KEY EVENT
	<p>receipt of necessary consents and approvals from the Government of India.⁴⁸</p> <p>(iii) The long stop date was revised as December 15, 2011⁴⁹</p>
July 11, 2011	<p>Twin Star acquired 191,920,207 equity shares constituting 9.976% of the Voting Capital of Cairn India from Cairn UK Sub by way of an off-market deal pursuant to the Agreement and an amendment agreement to the Agreement dated June 27, 2011.⁵⁰ Post the sale, the shareholding of Cairn UK Sub in Cairn India dropped to 51.531%⁵¹ of the Voting Capital, whereas the shareholding of Twin Star along with the PACs increased from the existing 18.455% to 28.431% of the Voting Capital.⁵²</p>
July 26, 2011	<p>The Government of India granted its approval to the transfer of controlling interest in Cairn India by Cairn UK Sub to Acquirer Group, subject to the following conditions:⁵³</p> <ul style="list-style-type: none"> (i) Parent financial and performance guarantees furnished by Cairn UK Parent in pursuance to relevant applicable Article(s) of the 7 NELP PSCs and 3 Pre-NELP PSCs, shall be substituted by parent financial and performance guarantees to be furnished by Vedanta Resources, which needs to be acceptable to the Government of India and should be in the form and substance set out in the PSC; (ii) Vedanta Resources to guarantee that the technical capability of Cairn India is and shall be kept undisturbed and ensure continued production of oil and gas as per approved field development plan from time to time. In case Vedanta Resources fails to perform as guaranteed then Government of India shall be entitled to stipulate additional conditions, as deemed fit, including change in operatorship of blocks; (iii) Vedanta Resources also shall give an undertaking that they shall ensure adherence to the approved field development plans and work programs; (iv) Cairn India and its affiliates shall provide the No Objection Certificate (NOC) obtained from their consortium partner(s) for each abovementioned blocks (except for Ravva (PKMG-1) and CB-OS/2 blocks) for the proposed transaction under the respective PSCs; (v) Necessary approvals from other regulatory bodies such as SEBI, on the proposed transaction to be obtained and submitted by Vedanta Resources; (vi) Necessary security clearance from Ministry of Home Affairs in favour of the

⁴⁸ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_280611.pdf, last visited on December 27, 2011

⁴⁹ [http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20\(Jan%202012\).pdf](http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20(Jan%202012).pdf); last visited on January 14, 2012

⁵⁰ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_130711_SAST.pdf, last visited on December 27, 2011

⁵¹ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_130711_SAST1.pdf, last visited on December 27, 2011

⁵² http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd1_130711_SAST.pdf, last visited on December 27, 2011

⁵³ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_080811.pdf, last visited on December 27, 2011

DATE	KEY EVENT
	<p>assignee, i.e. Vedanta Resources to acquire the shareholding shall be obtained and submitted by the said assignee;</p> <p>(vii) In respect of RJ-ON-90/1 block, the parties, i.e. Cairn India, Cairn Energy India Pty Limited (“CEIL”), Cairn Energy Hydrocarbons Limited (“CEHL”) and any other affiliate company of Cairn India; and Vedanta Resources and any other affiliate company of Vedanta Resources, shall agree and give an undertaking that the royalty paid by ONGC is cost recoverable by ONGC as contract cost, as per the provisions of the PSC; and</p> <p>(viii) In respect to RJ-ON-90/1 block, CEIL and CEHL shall withdraw the arbitration case relating to the dispute raised by them on payment of cess under the PSC.</p>
September 14, 2011	The shareholders of Cairn India approved through postal ballot, by way of ordinary resolution the conditions imposed by the Government of India. The resolution was approved with overwhelming majority vote of 97.29%.
December 6, 2011	The board of Vedanta Resources announced that applications have been made to the UK Listing Authority and the LSE for the re-admission to listing on the official list of the UK Listing Authority and to trade on the main market of the LSE of Vedanta Resources' 296,908,045 existing ordinary shares of USD 0.10 upon the cancellation of the listing of such shares in accordance with the requirements for reverse takeovers, which are applicable to the transaction under the UK listing rules. ⁵⁴
December 7, 2011	Sesa Goa acquired 24,307,241 equity shares (1.263% of Voting Capital) and its subsidiary Sesa Resources acquired 4,500,000 equity shares (0.233 % of Voting Capital) of Cairn India aggregating to approximately 1.496% of Voting Capital of Cairn India from Cairn UK Sub at an average price of INR 325 per share through a bulk deal ⁵⁵ on the BSE. With this acquisition Sesa Goa along with its subsidiary, Sesa Resources held 19.953% of the Voting Capital of Cairn India. ⁵⁶
December 8, 2011	Twin Star acquired 546,953,379 equity shares of Cairn India constituting 28.431% of the Voting Capital of Cairn India from Cairn UK Sub by way of an off-market deal pursuant to the Agreement and the amendment agreement to the Agreement dated June 27, 2011. With this acquisition Twin Star alone holds 38.408% of the Voting Capital, and together with Sesa Goa and Sesa Resources holds 58.361% of the Voting Capital of Cairn India. ⁵⁷ Also, the shareholding of Cairn UK Sub in Cairn India, post the sale to Twin Star, Sesa Goa and Sesa Resources, has decreased from 51.531% to 21.601% of the total share capital of Cairn India. ⁵⁸

⁵⁴ <http://www.londonstockexchange.com/exchange/news/market-news/market-news-detail.html?announcementId=11054924>, last visited on December 27, 2011

⁵⁵ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_091211_SAST1.pdf; last visited on December 27, 2011; In Form B filed by Sesa Goa and Sesa Resources under the SEBI (Prohibition of Insider Trading) Regulations, 1992, these transactions were termed as bulk deals.

<http://www.bseindia.com/qresann/news.asp?newsid={A1E951CA-4F51-47E9-92C4-86F00EC95433}>, last visited on December 27, 2011

⁵⁷ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_091211_SAST1.pdf; last visited on December 27, 2011.

⁵⁸ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_081211_SAST.pdf; last visited on December 27, 2011

DATE	KEY EVENT
	The readmission of Vedanta Resources' ordinary shares to listing on the official list of the UK Listing Authority and to trade on the LSE's main market for listed securities and commencement of dealings in such shares took place.

V. DEAL SUMMARY

1. How the acquisition consummated and what were the terms of the Agreement dated August 15, 2010?

Part of the acquisition was consummated pursuant to the terms of the Agreement, entered inter alia between Seller Group, Acquirers and Cairn India. Sesa Goa and Sesa Resources⁵⁹ were PAC, as far as this Deal is concerned.⁶⁰ The remaining part of the acquisition was by way of bulk deal on BSE⁶¹, whereby Sesa Goa purchased 10.396% of the Voting Capital from Petronas,⁶² and acquisition of 8.058% of the Voting Capital by Sesa Goa under Open Offer subject to the Takeover Code, 1997.

Bulk Deal

Bulk deal constitutes of all deals in a scrip (on an exchange) where the total quantity of shares bought / sold is more than 0.5% of the number of equity shares of the company listed on the exchange.⁶³ The quantitative limit of 0.5% can be reached through one or more deals executed during the day in the normal market segment.⁶⁴

Vide the Agreement, the Acquirers have agreed to acquire from Cairn UK Sub (either by itself or any person nominated by it (which may include the PAC)) such number of equity shares representing 51% of the Voting Capital. The number of shares acquired under the Agreement will be reduced by (a) and (b) below ("**Sale Shares**"):

- (a) the number of equity shares validly tendered in the Open Offer up to a maximum of 11% of the Voting Capital as on Closing Date, provided that the Sale Shares shall in no event be reduced below 40% of Voting Capital as on Closing Date pursuant to the adjustment under this sub-clause (a); and

⁵⁹Sesa Resources was added as a Person Acting in Concert by a corrigendum to the Public Announcement made on April 5, 2011, available at: <http://www.sebi.gov.in/takeover/cairindiacorrigen.pdf>, last visited on December 26, 2011

⁶⁰Notice of Postal Ballot issued to the shareholders of Cairn India on July 26, 2011 under Section 192A of the Companies Act, 1956.

⁶¹ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_210411_SAST.pdf, and http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_210411_SAST1.pdf; last visited on December 27, 2011

⁶² http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_091211_SAST1.pdf last visited on December 27, 2011;

⁶³Circular No. SEBI/MRD/SE/Cir-7 /2004 dated January 14, 2004, available online at <http://www.sebi.gov.in/circulars/2003/cirmrd072004.pdf>, last visited on December 28, 2011

⁶⁴Circular No. MRD/DoP/SE/Cir- 19 /05 dated September 2, 2005, available online at <http://www.sebi.gov.in/circulars/2005/mrdcir0192005.html>, last visited on December 28, 2011

- (b) At the election of the Acquirers, any transfer of equity shares by the Seller Group (other than the Sale Shares) for emergency funding reasons following severe financial difficulty prior to closing;

provided that, the aggregate of equity shares in the capital of Cairn India to be acquired pursuant to the Open Offer and the Agreement shall not be less than 51% of the Voting Capital as of Closing Date.

Cairn UK Parent to retain stake

Depending on the number of Cairn India shares sold pursuant to the Agreement, it was expected that Cairn UK Sub would have a residual interest of approximately between 10.6% and 21.6% of the Voting Capital of Cairn India.

Put and call options

The Acquirers and the Seller Group had also entered into put and call arrangements in relation to a part of the equity shares of Cairn India that may be retained by the Seller Group. The put and call obligations related to a number of the shares of Cairn India equal to the shortfall between the number of Sale Shares actually acquired by the Acquirers and 51% of the Voting Capital, subject to a maximum of 10% of Voting Capital of Cairn India. The first of these put and call options was exercisable after July 31, 2012 for a period of 6 months and the other after July 31, 2013 again for a period of 6 months, in both cases at an effective price per share of INR 405. Each option could be exercised in respect of a maximum of 5% of the voting capital on a fully diluted basis of Cairn India as at the date of exercise of the option. In approving the sale of Sale Shares of up to 51% of Cairn India, shareholders were also to approve the exercise of these reciprocal put and call arrangements.⁶⁵

Pre-emption rights and Right of First Refusal

In addition to the options mentioned above, if the Seller Group proposed to transfer any of the shares that they would continue to hold after closing, after the expiry of 6 months from closing, the Acquirers could exercise a 'right of first refusal' in respect to those shares at INR 405 per share. The Seller Group had also agreed to give the Acquirers a pre-emption right over any subsequent disposal of equity shares where such disposal would result in the recipient of the shares holding more than 20% of issued share capital of Cairn India.

Non-compete fees

Seller Group had given non-compete undertaking under the Agreement, covering the territories of India, Sri Lanka, Pakistan and Bhutan. For a period of three years, Seller Group agreed that they would not engage in the business of oil or gas extraction, its transport or processing and any other business which competes with the business of Cairn India in any of the specified territories. An

⁶⁵ Letter to the shareholders of Cairn UK Parent dated August 16, 2010, available at [http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20\(Final\).pdf?n=6663](http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20(Final).pdf?n=6663), last visited on December 28, 2011

amount of INR 50 per share, over and above the agreed consideration per share of INR 355, was agreed as the non-compete fees.⁶⁶

Break-up fee

Under the Agreement, Seller Group had agreed to pay Acquirers a break-up fee of 1% of the market capitalization of Cairn India (as on August 13, 2010), if the shareholders do not approve the Deal by the date agreed, or in case the Seller Group are in breach of obligation not to solicit competing proposals. The break-up fee was payable within 30 days of happening of the stated default.⁶⁷

2. Amendment date April 21, 2011: What changed?

By way of an amendment agreement dated April 21, 2011, the Acquirers and the Seller Group agreed that the Sale Shares shall be further reduced by 200 million equity shares acquired at any time prior to the Closing Date from any third party outside of the Open Offer. In other words, the Sale Shares will be deducted by the number of equity shares validly tendered in the Open Offer *and* 200 million equity shares acquired at any time prior to Closing Date from any third party outside of the Open Offer up to a maximum of 11% of the Voting Capital, provided that the Sale Shares shall in no event be reduced below 40% of Voting Capital pursuant to both such deductions.⁶⁸

Accordingly, the shares acquired from Petronas was reduced from the Sale Shares. Therefore, the floor of 40% Voting Capital would have to be met, after deducting both the stake acquired under the Open Offer and from Petronas.

On June 27, 2011 the parties to the Agreement entered into another amendment agreement whereby they agreed to:

- (i) Remove the provisions relating to non-compete fees; and
- (ii) Complete the Deal in two tranches, at a new price of INR 355 per share (after the removal of non-compete fees), as follows: (a) Initial sale of 10% of fully diluted share capital on or before July 11, 2011; (b) subsequent sale of fully diluted share capital, subject to applicable consents from government⁶⁹

⁶⁶ Letter to the shareholders of Cairn UK Parent dated August 16, 2010, available at [http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20\(Final\).pdf?n=6663](http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20(Final).pdf?n=6663), last visited on December 28, 2011

⁶⁷ *Id.*

⁶⁸ See Corrigendum to the Letter of Offer and Public Announcement, www.sebi.gov.in/takeover/cairn/corrigen3.pdf, last visited on December 27, 2011

⁶⁹ Announcement by Cairn UK Parent, June 27, 2011, http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_280611.pdf; *Vedanta to take 10 per cent stake as Cairn rejigs deal*, June 5, 2011, <http://www.deccanchronicle.com/channels/business/news/vedanta-take-10-cent-stake-cairn-rejigs-deal-124>, last visited December 23, 2011

3. What were the changes made to the Agreement?

To accommodate the concerns raised by SEBI, the clauses pertaining to put and call options and pre-emption rights were withdrawn by the parties.⁷⁰

VI. COMMERCIAL CONSIDERATIONS

“The first twelve words of Charles Dickens’ “A Tale of Two Cities” could possibly describe the affairs of Cairn India Limited in FY2011: “It was the best of times; it was the worst of times.” The year saw your Company performing remarkably well across various fronts; yet it faced an uncertain regulatory environment that delayed many activities and created significant anxieties.”

Mr. Rahul Dhir, Managing Director and CEO of Cairn India
(In his letter to the shareholders in Annual Report 2010-11)⁷¹

1. Why did Vedanta group choose to enter oil and gas sector?

Vedanta group’s strategy comprises four key approaches: (i) asset optimization and cost reduction; (ii) capacity expansion; (iii) consolidating its holdings; and (iv) acquisitions. Evidently, by entering into oil and gas sector, it seeks to leverage its *“transactional, project execution and operational skills and experience.”*⁷²

Further, owning captive energy resources such as oil and natural gas can definitely offer cost advantages. Industry analysts conclude that ‘even if operational or regulatory obstacles prevent captive usage, it could act as a hedge’. The commercial logic is that while higher energy prices can bring down the mining division’s profits, the same hike can shoot up the profits of the exploration division.⁷³

This, however, should be read in the context of the lukewarm response received by the Government of India during its last oil and gas exploration licensing rounds.⁷⁴ Perhaps, Vedanta group is counting on its ability to operate in sectors where politics and policy impact business⁷⁵, especially so in the home country of the promoter of the Vedanta group Mr. Anil Agarwal. Following the consummation of

⁷⁰ Announcement by Cairn UK Parent, April 7, 2011, http://www.bseindia.com/xml-data/corpfilings/AttachHis/Cairn_India_Ltd_070411.pdf, also see Letter of Offer; <http://www.sebi.gov.in/takeover/cairnlof.pdf>, last visited on December 28, 2011; Please see the section titled LEGAL AND REGULATORY CONSIDERATIONS *infra*.

⁷¹ Annual Report of Cairn India, June 25, 2011, available at: <http://www.cairnindia.com/IR/IRAnnualReports/fullar201011.pdf>, last visited on December 23, 2011.

⁷² Ravi Ananthanarayanan, *Vedanta goes down the beaten path*, August 15 2010, available at: <http://www.livemint.com/2010/08/15210618/Vedanta-goes-down-the-beaten-p.html>, last visited on December 28, 2011.

⁷³ *Id.*

⁷⁴ See *India: ninth round of oil and gas auctions only receives limited interest from overseas*, April 5, 2011, available at: <http://www.oilandgasobserver.com/commentary/india-ninth-round-of-oil-and-gas-auctions-only-receives-limited-interest-from-overseas/005470>, last visited on December 21, 2011.

⁷⁵ Ravi Ananthanarayanan, *Vedanta goes down the beaten path*, August 15 2010, available at: <http://www.livemint.com/2010/08/15210618/Vedanta-goes-down-the-beaten-p.html>, last visited on December 23, 2011.

the Deal, Mr. Anil Agarwal announced that Cairn India intends to double its production, with effective support from ONGC, and the production can go up to 240 thousand barrels, in 2012-2013.⁷⁶

Though its debut entry into oil and gas sector is said to have caught Vedanta's investors unaware, the move is not without precedents. BHP Billiton Ltd, a mining major, reaped 27% of its segment profit from petroleum exploration business in December 2009. Vale SA of Brazil, another mining giant, is also said to be aiming at diversifying its energy supplies by acquiring stakes in oil and gas exploration assets. It already owns stakes in around 20 exploration blocks.⁷⁷ Some analysts viewed Sesa Goa's move of acquiring 20% of the stake more surprising. Interestingly, by a few, it was attributed to the cash that had piled upon its books and lack of other opportunities.⁷⁸

2. Why did Vedanta group target Cairn India?

In the words of Mr. Anil Agarwal:

“Cairn India's Rajasthan asset is world class in terms of scale and cost, delivering strong and growing cash flow. The company has a proven management team and very significant further resource potential.”

Following are some of the key aspects of Cairn India's business model which Vedanta group might have thought it can benefit from:⁷⁹

- **Its position in India:** In partnership with the Government of India and state governments, regulators and key industry participants such as ONGC, Cairn India has been exploring and operating development and production assets in India for over 12 years.
- **Exploration expertise:** Cairn India has long exploration experience in India, having made 29 hydrocarbon discoveries since 1994. In 2004, Cairn India made the largest onshore crude oil discovery in India since 1985 when it discovered the Mangala field in Rajasthan. Since then, Cairn India has made 17 additional discoveries in the Rajasthan block. It has been an active participant in New Exploration Licensing Policy (“NELP”) licensing round.
- **Development and operational expertise:** Cairn India has a proven track record of developing hydrocarbon resources in India. Cairn India is also an established low cost operator in India in the field of exploration and development of oil fields.
- **Solidifies Vedanta's position:** In addition, Cairn India increases Vedanta group's existing significant presence in Rajasthan, where Vedanta group's zinc operations are located, and where Vedanta group is the largest tax payer and one of the largest private employers.⁸⁰

⁷⁶ONGC to support in doubling Cairn's capacity: Anil Agarwal, MONEYCONTROL.COM, available at: http://www.moneycontrol.com/news/business/ongctosupportdoublingcairncapacity_631129.html, last visited on December 28, 2011.

⁷⁷Id.

⁷⁸Ravi Ananthanarayanan & Pallavi Pengonda, *An exit option for Cairn shareholders*, Aug 16 2010, available at: <http://www.livemint.com/2010/08/16223402/An-exit-option-for-Cairn-share.html>; last visited on December 9, 2011.

⁷⁹Letter to the shareholders of Cairn UK Parent dated August 16, 2010, available at [http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20\(Final\).pdf?n=6663](http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20(Final).pdf?n=6663), last visited on December 9, 2011

3. What strategic benefits does Cairn UK Parent seek to reap from the Deal?

Unlocking the value

The board of Cairn UK Parent believes that the Deal delivers positive benefits in line with its strategic goals.⁸¹ Cairn UK Parent's strategy has always been "to add value for shareholders by establishing commercial reserves from strategic positions in high potential exploration plays and then to realize that value at the appropriate time." According to its directors, the completion of the first phase of the Rajasthan development represented a significant milestone for the Cairn group, with the project then producing approximately 125,000 barrels per day. The project is now materially de-risked, leading to creation of significant value for the shareholders of Cairn UK Parent. Therefore, the Cairn UK Parent board believed that it is an appropriate time to realize a significant part of that value, whilst maintaining exposure to the ongoing business through a retained shareholding, which is now approximately 22% of the fully diluted share capital of Cairn India.⁸²

Residual Interest

On January 10, 2012, the board of Cairn UK Parent issued notice for general meeting seeking authority from its shareholders to dispose of or reduce the aforementioned residual interest in Cairn India. It was pointed out that Cairn UK Parent's residual interest in Cairn India represents a substantial proportion of the group's assets and therefore, due to its size, the sale of any material part of the residual interest would be subject to shareholder approval under the Listing Rules (defined below). The prior approval from its shareholders, Cairn UK Parent board believed, would provide the necessary flexibility, if it so chose, to dispose of a part, and up to all of the residual interest in Cairn India in a way which delivers best value for shareholders. As the shares of Cairn India are listed and freely traded on the Indian stock exchanges, it was pointed out that the potential purchasers would expect to be able to purchase Cairn India shares at the prevailing market price on the basis of normal market terms. The board of Cairn UK Parent believed that the potential purchasers would be unlikely to be willing to enter into any agreement to purchase Cairn India shares which is conditional on shareholder approval, given the readily available alternative of making market purchases without such a condition. This residual interest disposal authority, if granted, would expire on January 30, 2013, unless renewed.⁸³

Interestingly, it appears that the parent guarantees provided by Cairn UK Parent have not been released yet. In addition, Cairn UK Parent is still awaiting the release of its parent guarantee in respect of a PSC for a block relinquished by Cairn India following the satisfaction of all conditions and obligations under the PSC by Cairn India.⁸⁴

⁸⁰ *Id.*

⁸¹ Letter to the shareholders of Cairn UK Parent dated August 16, 2010, available at [http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20\(Final\).pdf?n=6663](http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20(Final).pdf?n=6663), last visited on December 27, 2011

⁸² *Id.*

⁸³

[http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20\(Jan%202012\).pdf](http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20(Jan%202012).pdf); last visited on January 14, 2012

⁸⁴

[http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20\(Jan%202012\).pdf](http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20(Jan%202012).pdf); last visited on January 14, 2012

Future expansion plans

Following completion of the Deal, the Cairn group's principal focus will be to advance its exploration programme in its frontier basin positions in Greenland and continue to pursue its proven strategy of building shareholder value from growth opportunities.⁸⁵ If the strategy that Cairn UK Parent followed in case of Cairn India proves fruitful, years later, one might possibly anticipate a similar turn of events where Cairn UK Parent quits active participation in its operations in Greenland to create value for its shareholders, while maintaining some exposure to the de-risked business.

Return of cash to shareholders of Cairn UK Parent

Cairn UK Parent had announced that it proposes to return approximately USD 3.5 billion of the sale proceeds to its shareholders. The return of cash was expected to be made in a manner that will provide shareholders with an element of choice as to when and in what form they receive the cash.⁸⁶ Accordingly, on January 10, 2012, Cairn UK Parent issued a circular detailing how such "return of cash" will be structured, inter alia, other management of affairs. The return of cash is proposed to be made by means of a B share structure with a connected share capital consolidation, in terms of which each shareholder will receive:

- For each existing ordinary share of Cairn Energy held on February 3, 2012: 1 B share;
- For every 33 existing ordinary shares of Cairn Energy held on February 3, 2012: 13 "new ordinary shares" of Cairn Energy

The B shares will not be listed on the official list of the UK Listing Authority or admitted to trading on the London Stock Exchange. The new ordinary shares will be listed on the official list and admitted to trading on the London Stock Exchange and will replace the existing ordinary shares.

The circular requested the approval of shareholders for attendant share capital consolidation and return of cash, which if approved, granted 3 choices to certain B shareholders:

- Choice 1: Single B share dividend: Each B shareholder will receive a single dividend of £1.60 in respect of each of those B shares in respect of which election of this choice has been made;
- Choice 2: If the B shareholder validly elects for this choice in respect of all or some of her B shares, it is expected that those B Shares will be purchased by Morgan Stanley under an initial purchase offer on February 14, 2012 at £1.60 per B Share, free of all dealing expenses and commissions. Any such B shares purchased by Morgan Stanley under the initial purchase offer would, in turn, be purchased by Cairn UK Parent from Morgan Stanley and then cancelled.
- Choice 3: Morgan Stanley will make an offer to acquire such B shares during April 2012 at £1.60 per B Share, free of all dealing expenses and commissions. The shares purchased by Morgan Stanley under the further purchase offer will also be purchased by Cairn UK Parent and cancelled.

⁸⁵ *Id.*

⁸⁶ <http://dailypioneer.com/home/online-channel/business-a-finance/26278-vedanta-buys-out-cairns-india-subsiary.html>, last visited on December 21, 2011.

The aggregate amount proposed to be returned to shareholders as aforementioned is equivalent to approximately 60.6% of the market capitalization of the Cairn Energy at the close of business on January 6, 2012.

The effect of the share capital consolidation is that the existing ordinary shares will be replaced by the new ordinary shares so as to reduce the number of shares in issue to reflect the amount of cash to be returned to shareholders. The aim of this is to seek to make the market price of a Cairn India share comparable before and after the proposed return of cash, subject to normal market movements following the date of this document. The ratio used for the Share Capital consolidation has been set by reference to the closing middle-market price of £2.64 per existing ordinary share of Cairn UK Parent on January 6, 2012. As all ordinary shareholdings in Cairn UK Parent will be consolidated, shareholders' percentage holdings in the issued ordinary share capital of the Cairn UK Parent will (save in respect of fractional entitlements) remain unchanged immediately following the share capital consolidation.

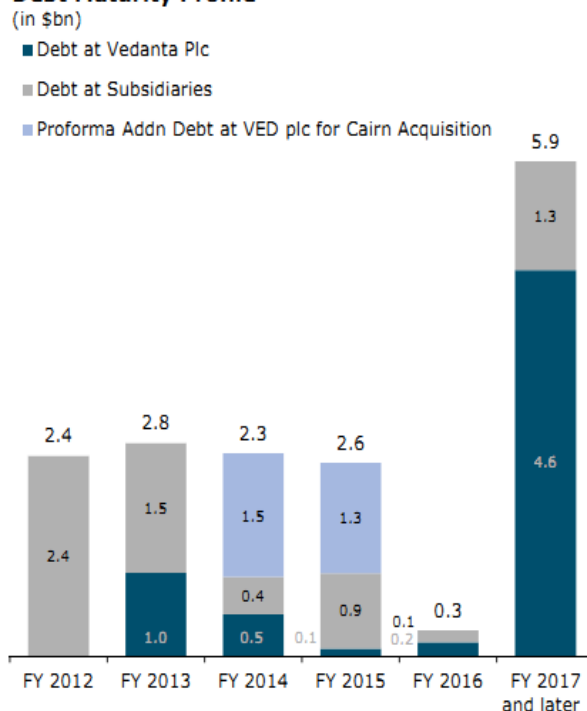
4. How is the Deal financed?

It may be pertinent to look at the Deal from a corporate finance perspective, considering that the Deal has left Vedanta Resources a company with substantial debt at the moment. The rationale behind Vedanta group's brave move could be a steady increasing trend in the prices of metal and crude oil.⁸⁷

Initially, it was announced that the financing of around USD 6 billion was structured in four tranches, with maturities of between 18 (eighteen) months and 3 (three) years.⁸⁸ Later, Vedanta Resources announced that it had planned to use proceeds of the IPO of its subsidiary Konkola Copper Mines, Zambia to repay USD 1.1 billion of the USD 6 billion debt availed from banks.⁸⁹ It was also announced that the following banks were participants in the financing:

- USD 1 billion bridge loan was arranged by Goldman Sachs, JP Morgan and Morgan Stanley Bank.

Debt Maturity Profile



⁸⁷ Ravi Ananthanarayanan & Pallavi Pengonda, *An exit option for Cairn shareholders*, August 16, 2010, available at: <http://www.livemint.com/2010/08/16223402/An-exit-option-for-Cairn-share.html>; last visited on December 9, 2011

⁸⁸ http://articles.economicstimes.indiatimes.com/2010-11-19/news/27590640_1_giant-rajasthan-block-vedanta-resources-plc-cairn-india; last visited on December 28, 2011.

⁸⁹ *Vedanta plans to use IPO money of Zambian unit KCM to part fund Cairn deal*; December 15, 2010, available at: <http://www.livemint.com/2010/12/15161546/Vedanta-plans-to-use-IPO-money.html>, last visited December 28, 2011

- Vedanta group has also got another bridge loan of USD 1.5 billion from Barclays Capital, Citigroup, Credit Suisse, The Royal Bank of Scotland and Standard Chartered Bank.
- A syndicated term loan of USD 3.5 billion, as originally announced, was to be obtained from Barclays Capital, Citigroup, Credit Suisse, Goldman Sachs, JP Morgan PLC, Morgan Stanley Bank, The Royal Bank of Scotland and Standard Chartered Bank.⁹⁰ However, it was subsequently reduced to USD 2.97 billion.⁹¹

Vedanta Resources also announced that it has raised USD 1.65 billion through private placement of bonds to part finance the acquisition.⁹² Citigroup, Barclays Capital, Credit Suisse, Royal Bank of Scotland and Standard Chartered Bank were the joint global coordinators and book runners for the issue, with Citigroup leading the execution.

According to Anil Agarwal, “we have enough dividends down the line in the company to throw the dividend to service all our debt. Out of the total, we have put 50% of our own money to acquire Cairn and the rest is funded through debt. We are very comfortable about it and have no plan to raise equity.”⁹³ He also termed the gearing of 40% as “comfortable”.⁹⁴

5. How did the Deal affect the prices of the shares of various corporate stakeholders?

Nothing is more eloquent on the investor perceptions that underlined the Deal, than how the share prices had reacted to the announcement of the Deal, the government intervention, the grant of approval and the final consummation of the Deal.



Announcement of the Deal:

Following the announcement of the Deal, Vedanta Resources plunged by 5.5% on the LSE.⁹⁵ Cairn UK Parent, at the same time, zoomed nearly 2% on the LSE.⁹⁶

⁹⁰ Vedanta plans to use IPO money of Zambian unit KCM to part fund Cairn deal; December 15, 2010, available at: <http://www.livemint.com/2010/12/15161546/Vedanta-plans-to-use-IPO-money.html>, last visited December 28, 2011.

⁹¹ Vedanta gets banks' commitment for loan, August 25, 2011, available at: <http://www.livemint.com/articles/2011/08/24182539/Vedanta-gets-banks8217-comm.html?atype=tp>, last visited December 8, 2011.

⁹² Vedanta raises \$1.65 billion to part-finance Cairn deal, May 27, 2011, available at: <http://www.livemint.com/2011/05/27180931/Vedanta-raises-165-billion-t.html>, last visited on December 9, 2011.

⁹³ ONGC to support in doubling Cairn's capacity: Anil Agarwal, MONEYCONTROL.COM, available at: http://www.moneycontrol.com/news/business/ongctosupportdoublingcairnscapa_631129.html, last visited on December 9, 2011.

⁹⁴ *Id.*

⁹⁵ Cairn India hits record high on BSE amid stake sale talks, ECONOMIC TIMES, August 13, 2010, available at: <http://m.economictimes.com/PDAET/articleshow/6306679.cms>, last visited on December 23, 2011.

⁹⁶ *Id.*

On August 9, 2010, the share prices of Cairn India fell to INR 328.5 per share, a fall which the analysts attributed to investor disappointment in the announced price, and possibly the perceived unfairness involved in the non-compete fees offered to Cairn UK Parent, who at all times had clarified that it would retain some stake in Cairn India.⁹⁷ On August 11, 2010, the prices rose, and by August 13, 2010, climbed over 5% to hit a record high of INR 358 per share on the BSE and settled, in the end, with a net gain of 4.36% at INR 355.45 per share. Analysts attributed such bullish tendency to the fact that even the lower end of the proposed Deal (USD 8 billion) valued Cairn India at USD 15.7 billion compared to market capitalization of USD 14.4 billion prevalent then.⁹⁸

Government's intervention and approval:

Analysts had believed that if royalties were made cost-recoverable and Cairn India were to foot out the 70% share of royalty payment, Cairn India's net asset value would fall by 14% to INR 337 per share, with crude oil prices at USD 100 per barrel.⁹⁹

On July 1, 2011, much to the street's surprise, the Cairn India stock shot up by around 5% to INR 326 per share, despite the stringent conditions proposed by the Indian government, as the news about its approval reduced the uncertainty surrounding the Deal.¹⁰⁰ It was predicted that ONGC would be the biggest beneficiary of the Indian government's intervention and that it could add INR 2.50 per share to ONGC's 2011-12 earnings per share of INR 30.5. Further, it would also stand to gain from recovering the past royalty payments.¹⁰¹ However, contrary to the predictions, ONGC increased its market capitalization only by INR 20.11 billion, significantly lower to an increase of INR 28.42 billion seen in Cairn India's market capitalization.¹⁰²

In August and September 2011, Cairn India shares didn't fare too well,¹⁰³ however, the shares of Cairn India surged by 4% to INR 288 per share as ONGC agreed to issue a no-objection certificate for the Deal.¹⁰⁴ It was reported on September 27, 2011 that owing to the nod given by the Indian government to the Deal, Cairn UK Parent shares were up by 4.9%. Shares of Vedanta Resources jumped 10.6%.¹⁰⁵

⁹⁷ Ravi Ananthanarayanan & Pallavi Pengonda, *An exit option for Cairn shareholders*, LIVEMINT, August 16 2010, available at: <http://www.livemint.com/2010/08/16223402/An-exit-option-for-Cairn-share.html>, last visited on December 28, 2011.

⁹⁸ *Cairn India hits record high on BSE amid stake sale talks*, ECONOMIC TIMES, August 13, 2010, available at: <http://m.economictimes.com/PDAET/articleshow/6306679.cms>, last visited on December 28, 2011.

⁹⁹ Ujjval Jauhari, *Cairn-Vedanta deal boost for ONGC*, BUSINESS STANDARD, July 5, 2011, available at: <http://www.business-standard.com/india/news/cairn-vedanta-deal-boost-for-ongc/441525/>, last visited on December 13, 2011

¹⁰⁰ *Cairn India: markets relieved that govt. has finally taken a decision*, LIVEMINT, July 4, 2011, available at: <http://www.livemint.com/articles/2011/07/03200111/Cairn-India-markets-relieved.html?type=tp> last visited on December 16, 2011

¹⁰¹ *Id.*

¹⁰² *Cairn-Vedanta deal boost for ONGC*, BUSINESS STANDARD July 5, 2011, <http://www.business-standard.com/india/news/cairn-vedanta-deal-boost-for-ongc/441525/> last visited on December 22, 2011.

¹⁰³ See Cairn India, Archives- Stock Prices, <http://www.bseindia.com/stockinfo/stockprc2.aspx>

¹⁰⁴ See *Cairn India surges by 4 per cent*, available at: <http://www.24dunia.com/english-news/shownews/0/Cairn-India-surges-by-4-per-cent/11746597.html>; last visited on December 28, 2011

¹⁰⁵ *Update 1-India's ONGC gives nod for Cairn-Vedanta deal*, REUTERS, available at: <http://uk.finance.yahoo.com/news/UPDATE-1-India-ONGC-gives-nod-targetukfocus-2754237541.html?x=0&.v=1>; last visited on December 23, 2011

Consummation of the Deal:

On December 5, 2011, the opening price of Cairn India shares was INR 315 per share. One may note that the price of equity shares of Cairn India, after steadily falling immediately following the consummation of the Deal, has now been rising. On December 21, 2011, it reached INR 318 per share, and by January 14, 2012, it had reached INR 336 per share.

On December 5, 2011, share prices of Vedanta Resources rose 2.85% while those in Cairn UK Parent increased by 1.8%. Though shares of Vedanta Resources fell on the subsequent days, a comparison of the same and the FTSE 100 index on a weekly basis showed the greater relative strength of Vedanta Resources, confirming investor appetite for the security. Analysts concluded that Vedanta Resources has been clearly attracting interest in the market.¹⁰⁶

6. Did the minority shareholders of Cairn India have any concerns arising from the Deal?

In August 2010, the board of Cairn India formed a special committee to ensure that the Deal between the Vedanta group and Cairn UK Parent is neither onerous nor prejudicial to the interest of Cairn India.¹⁰⁷ On February 10, 2011, board of directors at Cairn India passed resolutions opposing change in contract to make the company liable for payment of royalty and cess on oil produced from its Rajasthan fields. However, annual report for the year ending March 31, 2011 of Cairn India omits any mention in this respect. It was later reported that Cairn UK Parent would want Cairn India to accept the conditions imposed by the government.¹⁰⁸ Some analysts view this acquiescence as an action in disregard to the interests of the minority shareholders, to facilitate the exit of one shareholder.¹⁰⁹

Morgan Stanley in its report stated that “*while Cairn UK Parent and Vedanta control 80 per cent of voting rights, we believe the board of directors and minority shareholders may not accept these conditions.*”¹¹⁰ However, results of the voting conducted through postal ballot on the ordinary resolution to accept the conditions imposed by the India government in its approval letter dated July 26, 2011 proved the predictions wrong. The resolution was approved by the shareholders with a majority vote of 97.29%. Of the shareholders who voted, other than Cairn UK Sub and Vedanta group companies, 84.52% in number and 60.82% in value have voted in favour of accepting the conditions imposed by the India government.¹¹¹

¹⁰⁶ See London Stock Exchange, *Vedanta Resources Plc - Technical Analysis*, available at: <http://www.londonstockexchange.com/exchange/prices-and-markets/stocks/exchange-insight/technical-analysis.html?fourWayKey=GB0033277061GBGBXSET1>, last visited on December 23, 2011;

¹⁰⁷ Annual Report of Cairn India, June 25, 2011, available at: <http://www.cairnindia.com/IR/IRAnnualReports/fullar201011.pdf>, last visited on December 23, 2011

¹⁰⁸ http://articles.economicstimes.indiatimes.com/2011-08-23/news/29918638_1_mainstay-rajasthan-oil-block-uk-s-cairn-energy-plc-royalty-and-cess; last visited on December 28, 2011

¹⁰⁹ *Cairn India shows signs of accepting riders for Vedanta deal*, Livemint.com, July 20 2011, <http://www.livemint.com/2011/07/20152920/Cairn-India-shows-signs-of-acc.html>, last visited in December 23, 2011.

¹¹⁰ Kalpana Pathak, *Cairn-Vedanta deal riders upset global investors*, Business Standard, July 2, available at: <http://www.business-standard.com/india/news/cairn-vedanta-deal-riders-upset-global-investors/441272/>, last visited in December 23, 2011.

¹¹¹ *Cairn India Ltd - Intimation of Postal Ballot Results*; available at: <http://www.cairnenergy.com/NewsDetail.aspx?id=1730> ; last visited on December 28, 2011

It is now announced that Vedanta Resources, having stepped into the shoes of Cairn UK Parent, intends to pay dividends to the shareholders of Cairn India.¹¹² Apart from ONGC, it may be observed that Cairn India and its industry peers have minimal or no history of declaring dividends.¹¹³

VII. LEGAL AND REGULATORY CONSIDERATIONS

1. How does the Indian government and ONGC get to interfere in the Deal?

The Deal, which initially looked like a straight forward sale of shares, has since its announcement, been embroiled in a long drawn dispute and negotiations with the Government of India and ONGC.

The Indian Government had at the outset indicated that the Deal required its prior consent as Cairn India had signed PSCs with the Indian government for its oil and gas exploration blocks and as per the PSCs any change of ownership of Cairn India required prior approval of the Government of India.¹¹⁴

In all there were 10 (ten) exploration license areas in which Cairn India had acquired interests in. Of this, Cairn India maintained that only the 7 (seven) blocks under NELP required prior consent of the Government of India for transfer of control; and to that extent, they had applied for approval under Article 28.2 of the PSCs signed with the Indian government only for those 7 (seven) blocks.¹¹⁵

Article 28.2 of the Model PSC¹¹⁶

Article 28.2 of the Model PSC, as prescribed by the Ministry of Petroleum and Natural Gas, Government of India, deals with any change in the shareholding of the company. Article 28.2 of the Model PSC is as follows:

“Article 28.2: *In case of any change in the status of a Company or its shareholding resulting in a change in:*

- a) the control of the Company; or*
- b) its relationship with the company(ies) providing the guarantee under Article 29.1 (a) and 29.1(b);*

the Company shall seek the consent of the Government for assigning the Participating Interest under the changed circumstances and the provisions of this Article 28 shall apply, mutatis mutandis, to be obtaining of such consent.”

¹¹²ONGC to support in doubling Cairn's capacity: Anil Agarwal, MONEYCONTROL.COM, available at: http://www.moneycontrol.com/news/business/ongctosupportdoublingcairnscapa_631129.html, last visited on December 9, 2011.

¹¹³ Bonus and Dividends, Peer Group, Cairn India, available at: <http://bseindia.com/bseplus/StockReach/AdvanceStockReach.aspx?scripcode=532792>, last visited on December 12, 2011

¹¹⁴<http://www.livemint.com/2010/08/16122759/Vedanta-bids-to-control-Cairn.html>; <http://www.livemint.com/2010/08/17110527/Vedanta-sees-no-deal-hurdles-i.html>, last visited in December 28, 2011.

¹¹⁵<http://www.livemint.com/2010/09/13124331/Cairn-applies-for-government-a.html>, last visited in December 28, 2011.

¹¹⁶ Model PSC in respect of NELP VII is available at <http://petroleum.nic.in/nelp3.pdf>, last visited in December 28, 2011.

As regards, the other 3 (three) pre-NELP blocks – (i) Rajasthan block RJ-ON-90/1; (ii) the Ravva oil and gas field in the eastern offshore; and (iii) the Cambay basin CB/OS-2 gas fields off Gujarat coast; Cairn India maintained that it did not require prior consent of the Indian government as it did not have such provisions.¹¹⁷

With respect to ONGC, the issue emanated from the pre-emptive rights or the right of first refusal clause in the agreement with ONGC. Cairn UK Parent was of the view, as also conveyed to ONGC, that its decision to sell majority stake in Cairn India to Vedanta Resources did not trigger the state-owned firm's pre-emption rights as the Deal was at shareholder level involving sale of 40-51% shares of Cairn India, and there will be no change to, or assignment of, the participating interest in any of the 10 blocks held by Cairn India.¹¹⁸

However, ONGC rebutted by saying that change of control of Cairn India and acquisition of majority stake therein by Vedanta group amounts to an effective assignment/transfer of participating interest (or sale of stake in the asset like the Rajasthan block).¹¹⁹ A legal opinion sought by the finance ministry from the law ministry also stated that the change of control of Cairn India amounts to an indirect assignment or transfer of participating interest in its 10 blocks and so there is a need of the Indian Government as well as the partner's nod.¹²⁰

2. Why was the matter referred to Cabinet Committee on Economic Affairs (“CCEA”) for their approval?

Generally, CCEA approval is required when a foreign direct investment (FDI) Deal falls under the Government route and the total foreign equity inflow exceeds INR 12 billion. CCEA also considers proposals which may be referred to it by the Foreign Investment Promotion Board (“FIPB”), Ministry of Finance.

Since the Deal is a sale from a non-resident to another non-resident, which does not require prior FIPB approval and is under the automatic route, it is not clear as to under which regulation the matter was referred to CCEA for its approval. However, it appears that this requirement is emanating from the Government of India (Transaction of Business) Rules, 1961 (“**Transaction Rules**”)¹²¹. Rule 4 of the Transaction Rules provides that when the subject of a case concerns more than one department, no decision shall be taken or order issued until all such departments have concurred, or, failing such concurrence, a decision thereon has been taken by or under the authority of the Cabinet. Further, under First Schedule to the Transaction Rules, one of the functions of CCEA is to direct and coordinate all activities in the economic field including foreign investment, requiring policy decisions at the highest level. Probably therefore, considering the magnitude of the Deal and given its implications

¹¹⁷ <http://www.livemint.com/2010/09/13124331/Cairn-applies-for-government-a.html>, last visited in December 28, 2011.

¹¹⁸ <http://www.livemint.com/2010/11/04155130/Cairn-rebuts-ONGC8217s-clai.html>, last visited in December 28, 2011.

¹¹⁹ <http://www.livemint.com/2010/11/04155130/Cairn-rebuts-ONGC8217s-clai.html>, last visited in December 28, 2011.

¹²⁰ <http://www.livemint.com/2011/03/30173852/8216ONGC8217s-consent-ne.html>, last visited in December 28, 2011.

¹²¹ http://cabsec.nic.in/showpdf.php?type=allocation_businessrule, last visited on December 28, 2011

spanning across various ministries, the union petroleum minister stated in a press conference that the CCEA will decide upon the vexed Deal.¹²²

However, as it may happen, differences cropped in the CCEA on whether the Vedanta Resources, a mining group with no experience in oil should be given unconditional approval for buying a company that owns the nation's largest onland oil fields, or after attaching reasonable conditions pursuant to which the CCEA referred the matter to a ministerial panel.¹²³

3. What was the dispute on the conditions relating to royalty and cess arbitration imposed for the grant of approval to the Deal?

The CCEA on June 30, 2011 approved the Cairn UK Sub selling its 40% stake in Cairn India to Vedanta group subject to *inter alia* following conditions:¹²⁴

(a) Royalty: Cairn India, along with its subsidiary companies CEIL and CEHL, shall communicate an acceptance in respect of RJ-ON-90/1 block, that the royalty paid by ONGC is recoverable by ONGC as contract cost.

The issue in respect of royalty surfaced when ONGC raised a dispute that in respect of RJ-ON-90/1 block, the royalty payable under the PSC should be considered as contract cost for cost recovery purposes.

The CIG has a participating interest of 70%, and is the operator of Rajasthan block, in which ONGC holds the remaining 30% participating interest. On the one hand, Cairn India management is of the view that royalty is not a contract cost eligible for cost recovery because as per the provisions of the PSC, the cost of royalty should be borne by the licensee and the licensee under the PSC is ONGC.¹²⁵ They have also quoted Article 16.4 of their PSC for the Rajasthan fields that states "*Cairn shall not be liable to the government or a state government for payment of royalty...the cost of which shall be borne by the licensee (ONGC)*".¹²⁶

ONGC has, however, contended that the royalty payable under the Rajasthan block should be considered as contract cost for cost recovery purposed. Royalty is currently payable at 20% of the post well-head value of crude oil produced (on an ex-royalty basis), which translates to approximately 15% of the value received from the sale of crude oil.¹²⁷

¹²² <http://www.livemint.com/2011/02/15144457/CCEA-to-decide-on-Cairn-Vedant.html>, last visited in December 28, 2011.

¹²³ <http://www.livemint.com/2011/04/07111505/Cairn-India-stock-falls-as-Ved.html>, last visited in December 28, 2011.

¹²⁴ <http://www.livemint.com/2011/07/01165139/Cairn-India-profit-take-to-dip.html?d=1>, and intimation of postal ballot results of the Company given on September 14, 2011 to the BSE available at [http://www.bseindia.com/stockinfo/AnnPdfOpen.aspx?Pname=Cairn India Ltd 140911.pdf](http://www.bseindia.com/stockinfo/AnnPdfOpen.aspx?Pname=Cairn%20India%20Ltd%20140911.pdf), last visited in December 28, 2011.

¹²⁵ <http://www.cairnindia.com/IR/IRAnnualReports/fullar201011.pdf>, last visited in December 28, 2011.

¹²⁶ <http://www.livemint.com/2011/05/24164036/Cairn-contests-ONGC8217s-ro.html>, last visited in December 28, 2011.

¹²⁷ [http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn India Ltd 080811.pdf](http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn%20India%20Ltd%20080811.pdf), last visited on December 27, 2011

The Solicitor General of India (“SGI”), whose opinion was sought by the finance minister and the Group of Ministers, headed by Pranab Mukherjee, stated that Section 3.1 of Appendix C of the PSC provides that all costs incurred by the contractor in the form of duties, levies, fee, charges and any other assessments levied by the central or state government, are cost-recoverable. Further, the SGI said that “*the term ‘contractor’ has been defined in Clause 1.19(b) of the PSC as the company (Cairn India) and the nominee (ONGC), collectively. It is not disputed that ONGC, being the licensee / nominee, is a constituent of the contractor and therefore included within the meaning of term ‘contractor’*”.¹²⁸

Based on the PSC provision and legal advice received, CIG has been consistently of the view that royalty is payable by ONGC as a licensee and is not a contract cost and therefore, is not cost recoverable. The revenues are shared between CIG and ONGC in the proportion of their unrecovered contract costs. After recovery of all contract costs, the balance revenue, i.e. ‘Profit Petroleum’ is shared with Government of India based on the return on investment made by CIG (the higher the return achieved, the higher the percentage taken by the Government of India, subject to a maximum of 50%). The balance Profit Petroleum is shared between CIG and ONGC in the ratio of participating interest. In accepting ONGC’s payment of royalty as being treated cost recoverable, the revenues for CIG would be reduced to the extent of 70% of the royalty paid by ONGC. However, impact on CIG’s share of revenues shall reduce in future years to the extent of Government of India’s share of Profit Petroleum as the royalty thus paid shall also reduce the Profit Petroleum being shared with Government of India. During the year ended March 31, 2011, total revenues from the Rajasthan block were INR 125,518.5 million and the royalty paid by ONGC thereon in respect of 100% of the revenues was INR 18,320 million (equivalent to USD 407.1 million).¹²⁹

For ONGC, cost recovery of the royalty would mean that it will get USD 721.37 million over the life of the field as against a negative cash flow of USD 3.18 billion when the royalty was not cost recoverable.¹³⁰ However, the government take from the RJ-ON-90/1 block will come down to USD 3.6 billion from USD 5.188 billion as a result of royalty being made cost recoverable.¹³¹

(b) Cess Arbitration: Cairn India’s subsidiary companies CEIL and CEHL, in respect of RJ-ON-90/1 block, shall withdraw the cess arbitration initiated by them against the Government disputing their liability to pay cess, or tax, on their 70% share of oil from the Rajasthan fields.

The issue of cess arbitration arose when ONGC sent a claim notice to Cairn India to pay cess on oil produced from the Rajasthan block to the extent of Cairn India’s participating interest in this block, pursuant to which Cairn India had initiated arbitration proceedings against the Government of India and ONGC as it believed that the same should not be borne by Cairn India.¹³²

¹²⁸ <http://www.livemint.com/2011/05/24164036/Cairn-contests-ONGC8217s-ro.html>, last visited in December 28, 2011.

¹²⁹ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_080811.pdf, last visited on December 27, 2011

¹³⁰ <http://www.livemint.com/2011/07/01165139/Cairn-India-profit-take-to-dip.html>, last visited in December 27, 2011.

¹³¹ <http://www.livemint.com/2011/07/01165139/Cairn-India-profit-take-to-dip.html?d=1>, last visited in December 27, 2011.

¹³² <http://www.livemint.com/2011/07/20152920/Cairn-India-shows-signs-of-acc.html>, last visited in December 28, 2011.

During the year ended March 31, 2011, the total cess paid by the Company on production of oil and oil equivalents of 4.97 MMT from the Rajasthan block was INR 12,788.8 million (equivalent to USD 284.2 million).¹³³

Acceptance of the above riders would have reduced Cairn India's profit take from its prized Rajasthan oilfields over the approved life lasting 2020 from USD 7.43 billion to USD 5.75 billion that is by USD 1.68 billion.¹³⁴ Naturally, objections were raised by Cairn India / Vedanta Resources against these conditions imposed by the CCEA; but the CCEA overruled these objections by Cairn India / Vedanta Resources and held these will have to be met before the approval is granted for the proposed Deal.¹³⁵

4. Why were put option and call option arrangements removed from the Deal documents?

On April 20, 2011, SEBI issued a directive to Vedanta Resources and Cairn UK Parent to drop the arrangements in respect to the put and call option and pre-emption right from their agreements. It has taken the view that the put and call options are in violation of Notification No. SO 184(E) dated March 1, 2000 issued by SEBI since these do not conform to the requirements of a spot delivery contract nor with a contract of derivatives under Section 18A of the Securities Contract Regulation Act, 1956 ("SCRA").¹³⁶

SEBI has stated that since these options would be exercised on a future date, such Deal would not qualify as spot delivery contracts as defined in section 2(i) of SCRA.¹³⁷ These put/call options would not qualify as valid derivative contracts as per section 18A of the SCRA as these are exclusively entered into between two parties and not traded on stock exchanges and settled on the clearing

¹³³ http://www.bseindia.com/xml-data/corpfiling/AttachHis/Cairn_India_Ltd_080811.pdf, last visited on December 27, 2011

¹³⁴ Sources said the lower profits have been calculated at approved peak output of 175,000 barrels a day and considering a crude oil price of USD 70 per barrel. The net present value of Cairn India's loss of profitability is USD 1.39 billion, a little more than the USD 800 million concession in the purchase price that Vedanta has already got from Cairn UK Parent; <http://www.livemint.com/2011/07/01165139/Cairn-India-profit-take-to-dip.html>, last visited in December 28, 2011.

¹³⁵ <http://www.livemint.com/2011/07/01165139/Cairn-India-profit-take-to-dip.html?d=1>, last visited in December 28, 2011.

¹³⁶ Contracts in derivative:

Section 18A: Notwithstanding anything contained in any other law for the time being in force, contracts in derivative shall be legal and valid if such contracts are—

- (a) traded on a recognised stock exchange;
- (b) settled on the clearing house of the recognised stock exchange, in accordance with the rules and bye-laws of such stock exchange.

¹³⁷ Definitions:

"Section 2. In this Act, unless the context otherwise requires,

(i) "spot delivery contract" means a contract which provides for,—

- (a) actual delivery of securities and the payment of a price therefore either on the same day as the date of the contract or on the next day, the actual period taken for the despatch of the securities or the remittance of money therefore through the post being excluded from the computation of the period aforesaid if the parties to the contract do not reside in the same town or locality;
- (b) transfer of the securities by the depository from the account of a beneficial owner to the account of another beneficial owner when such securities are dealt with by a depository";

house of the recognized stock exchanges.¹³⁸ To solve this regulatory conundrum, parties agreed to remove the put and call arrangements between the Seller Group and the Acquirers.¹³⁹

Impact of SEBI's objection to the put/call options on the future of M&A transactions

In an Informal Guidance dated May 23, 2011, provided to Vulcan Engineers Limited ("**Vulcan Engineers**"),¹⁴⁰ SEBI has adopted the same approach. In that matter, an Italian financial company had the option to sell all its shares in Vulcan Engineers to another Italian company, starting from June, 2015 at a price pre-determined in accordance with certain criteria set out in the contract. This, according to SEBI, is not valid under the SCRA.

Though, it is very likely that this stand of SEBI would be challenged in courts soon, it remains to be seen how would the courts interpret the legality of call and put options.

For further detailed analysis on enforceability of put and call options, please refer to our articles / hotlines: (a) [Options, puts and the law](#),¹⁴¹ (b) [New Consolidated FDI Policy: Entry is welcome – Exit at our 'option'!](#),¹⁴² (c) [FDI Policy on Options in Equity Instruments Amended](#).¹⁴³

5. Why did Vedanta group agree to buy 10% share capital of Cairn India prior to government approval under the revised arrangement?

Under the revised arrangement, Vedanta group had agreed to buy only 10% shareholding of Cairn India without prior approval of the Indian government. It is not clear as to the exact reason for the purchase of such 10% stake pending government approval.

Though, *prima facie* it appeared that one of the reasons for such restructuring could emanate from the recently notified provisions relating to 'combination' of the Competition Act, 2002 which came into effect on June 1, 2011¹⁴⁴; however, since the 'combination' provisions only exclude transactions from its purview where binding document such as a share purchase agreement has been executed for the acquisition of shares before June 1, 2011, and the purchase of 10% stake which concluded on July 11, 2011¹⁴⁵ was pursuant to an agreement and amendment agreement entered into between the

¹³⁸ *Put/Call Options & Mandatory Buyback are invalid*, SEBI Updates, June 5, 2011, available at: <http://sebiupdates.blogspot.com/2011/06/putcall-options-mandatory-buyback-are.html>, last visited in December 27, 2011.

¹³⁹ Letter of Offer; <http://www.sebi.gov.in/takeover/cairnlof.pdf>, last visited on December 28, 2011

¹⁴⁰ Available at: <http://www.sebi.gov.in/informalguide/Vulcan/sebilettervulcan.pdf>, last visited in December 27, 2011.

¹⁴¹ http://www.nishithdesai.com/Media_Article/2009/Options%20puts%20and%20the%20law-Livemint.pdf

¹⁴² http://www.nishithdesai.com/New_Hotline/CorpSec/CORPSEC%20HOTLINE_Oct0311.htm

¹⁴³ http://www.nishithdesai.com/New_Hotline/CorpSec/CORPSEC%20HOTLINE_Nov0111.htm

¹⁴⁴ Please refer to our Hotline titled '*Indian Merger Control Regulations Finally Notified!!!*' for detailed analysis on the subject, available online at http://www.nishithdesai.com/New_Hotline/Competition/Competition_Law_hotline_May1311.htm, last visited on December 27, 2011.

¹⁴⁵ http://www.bseindia.com/stockinfo/AnnPdfOpen.aspx?Pname=Cairn_India_Ltd1_180711_SAST1.pdf, last visited on December 27, 2011

parties on August 15, 2010 and June 27, 2011 respectively, it doesn't seem likely that the 'combination' provisions would be reason for such sale.

Why part stake sale?

The probable reasons for the transfer of part stake in Cairn India could be (i) to provide the immediate funding requirements of Cairn UK Parent which was getting delayed on account of the riders imposed by the government; and (ii) such a purchase would increase the shareholding of Vedanta Resources in Cairn India to approximately 28.5% which would mean triggering of the statutory veto rights. Also, as per Mr. Anil Agarwal, Executive Chairman of Vedanta Resources, this initial 10% purchase is further demonstration of its commitment to India.¹⁴⁶

Why only 10%?

Since post the transfer of such 10% stake, the shareholding of Cairn UK Parent would still be approximately 52.2%, Cairn UK Parent would continue to remain the majority shareholder and retain control of Cairn India. Therefore, the pre-emptive rights of the government and ONGC do not get triggered as there was no change in the control; hence, this Deal could be concluded without their prior approval.

6. Can an amendment agreement trigger the combination provisions of the Competition Act?

The Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011 ("**Combination Regulations**") came into effect on June 1, 2011.

As per Regulation 31 of the Combination Regulations,

"The notice referred to under Section 6(2)¹⁴⁷ of the Competition Act, 2002 would be applicable, as follows:

- (a) for mergers or amalgamations referred to in clause (c) of section 5 of the Act, notice to be filed only in regard to proposals approved by the board of directors on or after the 1st day of June, 2011; and*
- (b) for acquisitions referred to in clause (a) of section 5 of the Act or acquiring of control referred to in clause (b) of section 5 of the Act, notice need to be filed only, where binding document(s) is executed, on or after the 1st day of June, 2011"*

From the above quoted provision, it appears that an acquisition pursuant to an amendment agreement entered into after June 1, 2011, may fall within the purview of regulation 31(b). However, since (i) the Agreement (dated August 15, 2010) (entered into prior to June 1, 2011), is also a binding

¹⁴⁶ Announcement of Cairn UK Parent to the BSE dated June 28, 2011 (released to the London Stock Exchange on June 27, 2011) available at: http://www.bseindia.com/stockinfo/AnnPdfOpen.aspx?Pname=Cairn_India_Ltd_280611.pdf, last visited on December 27, 2011

¹⁴⁷ S. 6(1) prohibits all mergers which causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and states that such combinations would be void. S. 6(2) states that any person who or which proposes to enter into a combination shall give notice to the Commission disclosing details of the said combination.

document for the acquisition of Sale Shares, and (ii) the total number of shares to be acquired has not been amended under the amendment agreement, instead the acquisition has been restructured to be carried out in two tranches by way of the amendment agreement; it seems unlikely that the combination provisions should trigger in this case.

Having said that, though the Deal has already been consummated, it remains to be seen if the Competition Commission of India will raise any eyebrows.

7. Why was RBI approval required for the Deal?

As per Regulation 10¹⁴⁸ of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 (“**TISPRO Regulations**”), a person resident in India who proposes to transfer to a person resident outside India any security by way of sale, is required to make an application to the RBI for its approval if the transfer falls within the provisions of the Takeover Code, 1997.

Since, in the instant case, transfer of 40% stake in Cairn India did trigger the Takeover Code, 1997, therefore, as per Regulation 10 of the TISPRO Regulations, prior approval of the RBI was required.

Restrictions of transfer of shares inter-se residents and non-residents liberalized

Recently, *vide* A.P. (DIR Series) Circular No. 43 dated November 4, 2011 (“**Circular**”), the RBI has relaxed the requirement of its approval for transfer of shares *inter-se* residents and non-residents.

Prior to the issue of the Circular, any transfer of shares from a resident to a non-resident where the Takeover Code, 2011 was applicable required prior approval of the RBI. Such approval requirement has now been done away with if the transfer of shares is in adherence with the pricing guidelines and documentation requirements as specified by the RBI.

¹⁴⁸Regulation 10 of the TISPRO Regulations: Prior permission of Reserve Bank in certain cases for transfer of security.

10. A. TRANSFER BY WAY OF GIFT OR SALE BY A PERSON RESIDENT IN INDIA

A person resident in India who proposes to transfer to a person resident outside India not being erstwhile OCBs:—

...

(c) any security by way of sale, shall make an application to the Reserve Bank for its approval if,

(i) the activity of the Indian company, whose securities are being transferred, falls outside the automatic route, and the approval of the FIPB has been obtained for the said transfer;

(ii) the activity of the Indian company whose securities are being transferred, falls under the financial services sector;

(iii) the transfer falls within the purview of the provisions of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997; and

(iv) the transfer is to take place at a price which falls outside the pricing guidelines specified by Reserve Bank, from time to time.

For further detailed analysis on liberalization on transfer of shares inter-se residents and non-residents, please refer to our hotline titled '[Liberalization of Restriction on Transfer of Shares Inter se Residents and Non-Residents](http://www.nishithdesai.com/New_Hotline/CorpSec/CORPSECHOTLINE_Nov1811.htm)'.¹⁴⁹

8. Why did Vedanta make an Open Offer under the Takeover Code, 1997?

Under the Takeover Code, 1997, the open offer requirements were triggered in the following three situations:

- (i) 15% shares or voting rights: When an acquirer acquires shares or voting rights which entitles it to exercise 15% or more of the voting rights in a listed company.¹⁵⁰
- (ii) Creeping acquisition limit: When an acquirer, who holds 15% or more, but less than 55% shares or voting rights in a company, acquires, additional shares or voting rights entitling him to exercise more than 5% of the voting rights of a company, in a given financial year.¹⁵¹
- (iii) Voting Control: When an acquirer acquires control over the target company, irrespective of whether or not there has been any acquisition of shares or voting rights.¹⁵²

¹⁴⁹ http://www.nishithdesai.com/New_Hotline/CorpSec/CORPSECHOTLINE_Nov1811.htm

¹⁵⁰ Regulation 10 of the Takeover Code, 1997: No acquirer shall acquire shares or voting rights which (taken together with shares or voting rights, if any, held by him or by persons acting in concert with him), entitle such acquirer to exercise 15% or more of the voting rights in a company, unless such acquirer makes a public announcement to acquire shares of such company in accordance with the Takeover Code.

¹⁵¹ Regulation 11 of the Takeover Code, 1997: (1) No acquirer who, together with persons acting in concert with him, has acquired, in accordance with the provisions of law, 15 per cent or more but less than fifty five per cent (55%) of the shares or voting rights in a company, shall acquire, either by himself or through or with persons acting in concert with him, additional shares or voting rights entitling him to exercise more than 5% of the voting rights, with post acquisition shareholding or voting rights not exceeding fifty five per cent., in any financial year ending on 31st March unless such acquirer makes a public announcement to acquire shares in accordance with the regulations.

(2) No acquirer, who together with persons acting in concert with him holds, fifty-five per cent (55%) or more but less than seventy-five per cent (75%) of the shares or voting rights in a target company, shall acquire either by himself or through or with persons acting in concert with him any additional shares entitling him to exercise voting rights or voting rights therein, unless he makes a public announcement to acquire shares in accordance with these Regulations:

...

Explanation. — For the purposes of regulation 10 and regulation 11, acquisition shall mean and include,—

- a. direct acquisition in a listed company to which the regulations apply;
- b. indirect acquisition by virtue of acquisition of companies, whether listed or unlisted, whether in India or abroad.

¹⁵² Regulation 12 of the Takeover Code, 1997: Irrespective of whether or not there has been any acquisition of shares or voting rights in a company, no acquirer shall acquire control over the target company, unless such person makes a public announcement to acquire shares and acquires such shares in accordance with the regulations:

Provided that nothing contained herein shall apply to any change in control which takes place in pursuance to a special resolution passed by the shareholders in a general meeting:

Provided further that for passing of the special resolution facility of voting through postal ballot as specified under the Companies (Passing of the Resolutions by Postal Ballot) Rules, 2001 shall also be provided.

Explanation — For the purposes of this regulation, acquisition shall include direct or indirect acquisition of control of target company by virtue of acquisition of companies, whether listed or unlisted and whether in India or abroad.

Since, in the instant case Vedanta group was acquiring 40% stake in Cairn India from Cairn UK Sub, as per Regulation 10 of the Takeover Code, 1997 (*item (i) above*), Vedanta group was required to make an open offer.

9. Can an acquirer acquire shares of the target company during the open offer period?

Regulation 22(17) of the Takeover Code, 1997 provides that where an acquirer has acquired any shares in terms of Regulation 20(7) at a price equal to or less or more than the offer price, he shall *inter alia* disclose the number, percentage, price and the mode of acquisition of such shares to the stock exchanges on which the shares of the target company are listed.

Regulation 20(7) which deals with offer price, provides that where the acquirer has acquired shares in the open market or through negotiation or otherwise, after the date of public announcement at a price higher than the offer price stated in the letter of offer, then, the highest price paid for such acquisition shall be payable for all acceptances received under the offer. But the proviso to regulation 20(7) provides that no such acquisition shall be made by the acquirer during the last seven working days prior to the closure of the offer.

Therefore, from the above it appears that an acquirer can acquire the shares of the target company during the offer period; however, if the acquisition price is higher than the open offer price, such acquisition cannot be done during the last seven working days prior to the closure of the offer.

Since, Sesa Goa had acquired 10.396% of the total capital of Cairn India from Petronas at a price of INR 331 by way of bulk deal on April 19, 2011, it was well within the open offer price of INR 355, and therefore, compliant with the abovementioned regulations of Takeover Code, 1997.

Position under the Takeover Code, 2011

Under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (“**Takeover Code, 2011**”), as per proviso to regulation 18, an acquirer cannot acquire or sell any shares of the target company during the period between three working days prior to the commencement of the tendering period and until the expiry of the tendering period. Tendering period is the period within which shareholders tender their shares in acceptance of an open offer to acquire shares made under the Takeover Code, 2011.

10. What impact could the new Takeover Code, 2011 have on the Deal?

SEBI has on September 23, 2011 notified the Takeover Code, 2011, which came into force on the thirtieth day from the date of its publication in the Official Gazette.¹⁵³

Takeover Code

Please refer to our hotline titled ‘[Indian Takeover Regulations overhauled!](#)’,¹⁵⁴ dated August 4, 2011 for detailed analysis of the key recommendations which have been incorporated in the Takeover Code.

¹⁵³ Takeover Code, available at http://www.sebi.gov.in/cms/sebi_data/attachdocs/1316778211380.pdf, last visited on December 27, 2011

Amongst others, some of the key revisions relevant here under the new Takeover Code, 2011 are as follows:

- (i) Initial trigger of the Takeover Code, 2011: The first threshold for triggering the Takeover Code, 2011, requiring the acquirer to make a mandatory open offer is increased from 15% to 25% of the voting rights in the target company.
- (ii) Non-compete fee: The extant provision permitting payment of non-compete fee up to 25% of the offer price to the exiting promoters of the target company, in addition to the offer price stands deleted. The promoters of the target company cannot now be paid any additional consideration in comparison to the public shareholders, as non-compete fees.
- (iii) Open offer size: The minimum size of the mandatory open offer prescribed under the Takeover Code, 1997 has been increased from 20% to 26% of the voting capital of the target company.

The pertinent question here is that, since the actual transfer of approximately 30% stake in Cairn India had not been consummated until the introduction of the Takeover Code, 2011, did it mean that Vedanta group would have been required to make a fresh offer for the incremental mandatory open offer size? The answer is 'No'.

As per Regulation 35 of the Takeover Code, 2011, anything done or any action taken or purported to have been done or taken under the Takeover Code, 1997 prior to its repeal, shall be deemed to have been done or taken under the corresponding provisions of the Takeover Code, 2011 or shall remain unaffected as if the repealed regulations had never been repealed. Therefore, Vedanta group could continue with the existing offer it had made and was not required to make a fresh offer under the Takeover Code, 2011.

11. Why was the approval of the shareholders of Sesa Goa and Sesa Resources required to consummate the Open Offer pursuant to Section 372A of the Act?

The Letter of Offer provided that the Open Offer was conditional upon receipt of approvals from the shareholders of Sesa Goa and Sesa Resources pursuant to Section 372A of the Act.¹⁵⁵

Section 372A of the Act provides that no company shall, directly or indirectly, acquire by way of subscription, purchase or otherwise the securities of any other body corporate; exceeding sixty percent of its paid-up share capital and free reserve, or one hundred percent of its free reserves, whichever is more.

Where the aggregate of the loans and investments so far made, the amounts for which guarantee or security so far provided to or in all other bodies corporate, along with the investment proposed to be made the board, exceeds the aforesaid limits, no investment shall be made unless previously authorised by a special resolution passed in a general meeting.

¹⁵⁴ http://www.nishithdesai.com/New_Hotline/M&A/M&A%20Hotline_Aug0411.htm

¹⁵⁵ <http://www.sebi.gov.in/takeover/cairnlof.pdf>, last visited on December 27, 2011

It appears that the aforesaid limits could have exceeded in case of purchase of shares of Cairn India by Sesa Goa and Sesa Resources, hence, the above two companies procured a special resolution from the shareholders to effect the purchase of shares.

12. What are the corporate governance issues with respect to the interests of the minority shareholders against the backdrop of Deal?

The approval of the shareholders for concluding the Deal, which was, in turn conditional on the acceptance of conditions imposed by CCEA was obtained by way of a postal ballot under Section 192A of the Act, read with Companies (Passing of the Resolution by Postal Ballot) Rules, 2011. The resolution has the effect of an ordinary resolution passed in a general meeting. As mentioned earlier, the Deal was approved by an overwhelming majority. Additionally, the Deal, as far as the PACs are concerned, was also subject to the shareholders' approval under Section 372A of the Act (dealing with inter-corporate loans and investments) which approvals were also obtained.

13. Do the actions of the government violate India's obligations under Bilateral Investment Treaty (BIT) with United Kingdom?

It is possible that they do violate these obligations, if in facts and circumstances it is proven that the treatment afforded to Cairn UK Parent's investment is not fair, equitable and non-compliant in terms of Article 3, Article 4 and Article 7 of agreement entered into between India, UK and Northern Ireland for the promotion and protection of investments. For further analysis of the Deal from this perspective, click [here](#).¹⁵⁶

14. Was the non-compete fee justifiable in the facts of the Deal?

Vedanta Resources offered to pay INR 405 per share to Cairn UK Parent, i.e. INR 50 per share over and above the price offered to minority shareholders. Analysts are of the opinion that the payment of non-compete fees is not equitable in view of the Cairn UK Parent's proposed expansion plans and continued stake in Cairn India. As mentioned earlier, the provision of non-compete fees has been withdrawn. It yet warrants a glance into it as this has been one of the most debated parts of the Deal.

Securities Appellate Tribunal ("**SAT**"), in the case of Tata Tea,¹⁵⁷ has affirmed the validity of a non-compete fee in cases where the outgoing sellers are capable of offering competition to the business of the target company. Consequently, where there is a legitimate non-compete obligation and the non-compete fee does not exceed 25% of the offer price, there is no obligation on the acquirer to pay a non-compete consideration to the public shareholders of the target company.¹⁵⁸

¹⁵⁶ http://www.nishithdesai.com/Media_Article/2011/Cairn_Vedanta%20Deal_Vccircle.pdf

¹⁵⁷ Tata Tea Ltd. vs. Securities and Exchange Board of India and anr., [2010] 103 SCL 140

¹⁵⁸ Paragraph 6 of the Judgment: "The recommendations made by the Bhagwati Committee clearly recognize the legitimacy of the non-compete fee payable to the outgoing sellers. Regulation 20(8) based on these recommendations puts a cap on such payments so that an acquirer could not reduce the cost of acquisition through public offer thereby depriving the public shareholders of their legitimate dues. When examining the validity of the non-compete fee, the question to be addressed is whether the outgoing sellers are capable of providing competition to the business alone or in association with third parties and not whether the business was dependent on the outgoing sellers... Section 27 of the Contract Act recognises that non-compete agreements are not in restraint of trade if the restrictions placed are reasonable."

Later, in the case of *E-Land Fashion China Holdings Limited v. Securities and Exchange Board of India*¹⁵⁹, SAT upheld the decision in Tata Tea case referred to above.

However, given that Cairn UK Parent has chosen to retain a significant interest in Cairn India, and that its focus now, is to develop exploration potential in Greenland, it is opined that Cairn UK Parent is not a potential competitor to Cairn India's business. Hence, the payment of non-compete fees was largely viewed as unjustified. One must also note that the existing management is being retained in Cairn India. Ultimately, whether the payment of non-compete fee is justified or not depends on the facts and circumstances of a particular case.

Position under the Takeover Code, 2011

The Takeover Regulations Advisory Committee¹⁶⁰ recommended that the non-compete fee should be completely done away with and this proposal has been accepted by SEBI and have been incorporated in Takeover Code, 2011.

15. Did the Deal trigger any provisions of the Listing Rules of UK Listing Authority for Vedanta Resources and Cairn UK Parent?

Vedanta Resources

Vedanta Resources in its announcement dated August 16, 2011¹⁶¹ stated that the Deal, if completed, would be classified as a reverse takeover of Vedanta Resources under the listing rules of the UK Listing Authority. The listing rules of the UK Listing Authority ("**Listing Rules**") defines a 'reverse takeover' as a transaction consisting of an acquisition by a listed company of a business, an unlisted company or assets where any percentage ratio is 100% or more or which would result in a fundamental change in the business or in a change in board or voting control of the listed company.¹⁶²

The Listing Rules further state that a listed company must, in relation to a reverse takeover, comply with the Class 1 requirements¹⁶³ for that transaction.¹⁶⁴ As per Rule 10.5.1, in relation to a Class 1 transaction, a listed company is required, *inter alia*, to send an explanatory circular to its shareholders and obtain their prior approval in a general meeting for the transaction.

Further, under Rule 10.6.2, when a listed company completes a reverse takeover, the Financial Services Authority ("**FSA**") of UK generally cancels the listing of its equity shares and the company is required to re-apply for the listing of the equity shares and satisfy the relevant requirements for listing, subject to certain exceptions and conditions.¹⁶⁵ Accordingly, UK FSA cancelled the equity shares of

¹⁵⁹ Appeal No. 27 of 2011, Date of decision: 24.05.2011, available at: <http://www.sebi.gov.in/satorders/eland.pdf>

¹⁶⁰ Available at: <http://www.sebi.gov.in/commreport/tracreport.pdf>, last visited on December 27, 2011

¹⁶¹ http://www.vedantaresources.com/uploads/vedrelease_final.pdf, last visited on December 27, 2011

¹⁶² Rule 10.2.2, Listing Rules, available at: <http://fsahandbook.info/FSA/html/handbook/LR/10/2>, last visited on December 27, 2011

¹⁶³ <http://fsahandbook.info/FSA/html/handbook/LR/10/5#D185>, last visited on December 27, 2011

¹⁶⁴ Clause 10.6.1, Listing Rules, <http://fsahandbook.info/FSA/html/handbook/LR/10/6>, last visited on December 27, 2011

¹⁶⁵ Clause 10.6.2, Listing Rules, <http://fsahandbook.info/FSA/html/handbook/LR/10/6>, last visited on December 27, 2011

Vedanta Resources from the official list and from trading on the LSE at the request of Vedanta Resources on December 8, 2011.¹⁶⁶

Cairn UK Parent

Cairn UK Parent in its announcement dated August 16, 2011¹⁶⁷ stated that the Deal, if completed, would constitute a Class 1 transaction under the Listing Rules. As mentioned above, in case of a Class 1 transaction, a listed company is required, *inter alia*, to send an explanatory circular to its shareholders and obtain their prior approval in a general meeting for the transaction.

VIII. TAX CONSIDERATIONS

1. What are the tax implications of the sale of shares of Cairn India by Cairn UK Sub in India?

Since, as per Article 14¹⁶⁸ of the “*Agreement for avoidance of double taxation and prevention of fiscal evasion with United Kingdom of Great Britain and Northern Ireland*”, each contracting state may tax capital gains in accordance with the provisions of its domestic law; therefore, India has the right to tax the capital gains arising out of sale of shares of Cairn India by Cairn UK Sub.

Section 45 of the Income Tax Act, 1961 (“**IT Act**”) provides for capital gains tax on transfer of shares of an Indian company. Such capital gains are deemed to be long term capital gains where the shares have been owned and held by the transferor for a period of more than 12 months.¹⁶⁹

Assuming, the shares of Cairn India have been held by Cairn UK Sub for more than a year, the sale of shares of Cairn India by Cairn UK Sub on the floor of the stock exchange would not be subject to any long term capital gains tax in India, provided the applicable securities transaction tax is paid.¹⁷⁰

However, for the transfer of major chunk of shares of Cairn India by Cairn UK Sub, which took place off the floor, Cairn UK Sub could be subject to a capital gains tax of 10%¹⁷¹ without indexation.¹⁷²

¹⁶⁶ Notice of Cancellation of Listing from the Official List, December 8, 2011, available at: <http://www.londonstockexchange.com/exchange/news/market-news/market-news-detail.html?announcementId=11056684>, last visited on December 12, 2011.

¹⁶⁷ [http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20\(Final\).pdf?n=6663](http://www.cairnenergy.com/uploadedFiles/Media_and_News/News/Articles/16.08.10%20-%20Cairn-Vedanta%20(Final).pdf?n=6663), last visited on December 27, 2011

¹⁶⁸ ARTICLE 14 - Capital Gains - 1. Except as provided in Article 8 (Air Transport) and 9 (Shipping) of this Convention, each Contracting State may tax capital gains in accordance with the provisions of its domestic law.

¹⁶⁹ Section 2(42A) read with Section 2(29A) of the IT Act.

¹⁷⁰ Section 10(38) of the IT Act.

¹⁷¹ Unless specifically otherwise provided, all tax rates mentioned in this Lab shall be exclusive of cess and surcharges

¹⁷² Section 112 of the IT Act

112. (1) Where the total income of an assessee includes any income, arising from the transfer of a long-term capital asset, which is chargeable under the head “Capital gains”, the tax payable by the assessee on the total income shall be the aggregate of,—

...

(c) in the case of a non-resident (not being a company) or a foreign company,—

(i) the amount of income-tax payable on the total income as reduced by the amount of such long-term capital gains, had the total income as so reduced been its total income; and

(ii) the amount of income-tax calculated on such long-term capital gains at the rate of twenty per cent;

In the recent Authority for Advanced Ruling (“AAR”)¹⁷³ in relation to the off the floor transfer of shares of an Indian listed company, the AAR held that the applicant is not eligible to avail the benefit of lower rate of tax of 10% on the long term capital gains in case of transfer of listed shares.

The reason, for the denial of the reduced tax rate, it seems, is that since, as the second proviso to section 48¹⁷⁴ is not applicable to non-residents who are covered by the first proviso to section 48, the proviso to section 112 should also not apply to the non-residents and that the eligibility to avail benefit of indexation under second proviso to section 48 is a sine qua non to avail the benefit of lower rate of tax under the proviso to section 112.

Further, as it happens, the AAR ruling was in respect of an application by Cairn UK Sub, albeit, for a different transaction pertaining to sale of shares in Cairn India by Cairn UK Sub to Petronas Corporation International Limited. Though, a ruling of AAR is binding only on the applicant and on the concerned Commissioner of Income Tax and that too in relation to a specific transaction, and it is not a binding precedent; however, if such a view has been adopted by the AAR in one matter, it may be possible that the same view may be adopted for future transactions as well.

2. What are the tax implications of the sale of shares of Cairn India by Cairn UK Sub in UK?

The UK holding company regime exempts capital gains realised by a holding company upon disposition of substantial shareholdings. As Cairn UK Sub is the parent of Cairn India, there is a

...

Provided that where the tax payable in respect of any income arising from the transfer of a long-term capital asset, being listed securities or unit or zero coupon bond, exceeds ten per cent of the amount of capital gains before giving effect to the provisions of the second proviso to section 48, then, such excess shall be ignored for the purpose of computing the tax payable by the assessee.

¹⁷³ http://aarrulings.in/it-rulings/uploads/pdf/1312261455_cairn-ruling.pdf, last visited on December 27, 2011

¹⁷⁴ The relevant provision of Section 48 reads as follows:

48. The income chargeable under the head “Capital gains” shall be computed, by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amounts, namely :—

- (i) expenditure incurred wholly and exclusively in connection with such transfer;
- (ii) the cost of acquisition of the asset and the cost of any improvement thereto:

Provided that in the case of an assessee, who is a non-resident, capital gains arising from the transfer of a capital asset being shares in, or debentures of, an Indian company shall be computed by converting the cost of acquisition, expenditure incurred wholly and exclusively in connection with such transfer and the full value of the consideration received or accruing as a result of the transfer of the capital asset into the same foreign currency as was initially utilised in the purchase of the shares or debentures, and the capital gains so computed in such foreign currency shall be reconverted into Indian currency, so, however, that the aforesaid manner of computation of capital gains shall be applicable in respect of capital gains accruing or arising from every reinvestment thereafter in, and sale of, shares in, or debentures of, an Indian company :

Provided further that where long-term capital gain arises from the transfer of a long-term capital asset, other than capital gain arising to a non-resident from the transfer of shares in, or debentures of, an Indian company referred to in the first proviso, the provisions of clause (ii) shall have effect as if for the words “cost of acquisition” and “cost of any improvement”, the words “indexed cost of acquisition” and “indexed cost of any improvement” had respectively been substituted:

possibility that no tax would be levied in the UK, subject to satisfaction of applicable conditions under UK law.

3. What are the tax implications of the sale of shares of Cairn India by Petronas in India?

The India-Malaysia double tax treaty does not contain a provision in relation to capital gains. However, under Article 22 pertaining to 'Other Income', it is specified that where items of income are not expressly mentioned in the treaty, they shall be taxable only in the state of residence unless such items are considered to be derived from sources in the state of source.

In this case, if Petronas sells shares in Cairn India, the income from disposition of shares of an Indian company would be considered to have its source in India as per section 9(1)(i) of the IT Act. Therefore, the Indian tax implications for the non-resident Petronas should be as discussed above in Question 1 under this Section VIII. Malaysia only taxes specified kinds of capital gains and there is a possibility that there should be no Malaysian tax on Petronas on the disposition of equity shares.

IX. EPILOGUE

A Deal that took almost 16 (sixteen) months to see the light of the day had been marred with political upheaval, endless commercial transformations and complex interplay of legal and regulatory conundrums; however, hats off to the perseverance of one man – Mr. Anil Agarwal, who, despite all the highs and lows, maintained his patience and saw the brighter side of getting this Deal through and found way into a new sector in a thumping fashion.

Knowing the stakes involved and an industry that can have foremost impact on the economy of the country, one must give it to the Government of India in taking its course in raising the green flag for the Deal to cross the victory line. However, laying the map for future M&A transactions, the bigger concern lies, not in the decision, but in the decision making process. The concern lies in the propriety of government's appearance as an 'umpire'. The cumulative delay that surrounded the Deal made it "*selectively problematic to do business in India*", opined International Finance Corporation, an investor in Cairn India and a member of the World Bank group.¹⁷⁵ Incidentally, (nonetheless interestingly), in July 2011, when Sir Bill Gammell stepped down from his chief executive position to the position of non-executive chairman of Cairn UK Parent, its board of directors had decided to award him with an incentive package worth up to £3.5 million if the Deal was completed successfully by December 15, 2011 given his longstanding relationships with government of India. Sir Bill Gammell having achieved that goal, Cairn UK Parent has now sought the approval of its shareholders to keep this promise.¹⁷⁶

In fact, the gravity of the Deal was so huge that it saw a rare move by Mr. David Cameron, Prime Minister of United Kingdom who wrote to Mr. Manmohan Singh, Prime Minister of India, specifically addressing the deadlock that the Deal encountered. Mr. Cameron highlighted the need for greater transparency and predictability in India's policy environment to enhance trade and investment

¹⁷⁵ James Lamont, Vedanta's Cairn India deal hailed, FINANCIAL TIMES, December 5, 2011, available at: <http://www.ft.com/cms/s/0/f43e2abc-1efd-11e1-ab49-00144feabdc0.html#axzz1g7UsONLQ>, last visited on December 10, 2011.

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[http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20\(Jan%202012\).pdf](http://www.cairnenergy.com/uploadedFiles/Investors/Downloads/Proposed%20Return%20of%20Cash%20to%20Shareholders%20Circular%20(Jan%202012).pdf); last visited on January 14, 2012

between the two countries. Though the letter should be read as an attempt to bring a sharper commercial edge to British diplomacy, it highlighted certain concerns shared by investors across the globe, including the landmark Vodafone case.

X. CONCLUDING REMARKS

As you would be aware, we have been providing regular information on latest legal and regulatory developments. Publishing M&A Lab is our initiative to provide you knowledge based analysis and more insight on latest and landmark M&A deals.

You can direct your views / comments / suggestions on our initiative to siddharth.shah@nishithdesai.com, nishchal.joshi@nishithdesai.com, sambhav.ranka@nishithdesai.com, deepak.jodhani@nishithdesai.com and surya.binoy@nishithdesai.com.

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