

M&A Hotline

August 04, 2011

INDIAN TAKEOVER REGULATIONS OVERHAULED!

SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 ("**Takeover Code**") now stands overhauled. Our earlier hotline, "*Indian Takeover Regulations up for Overhaul!*" analyses in detail, the recommendations made by the Takeover Regulations Advisory Committee ("**TRAC**") in its report dated July 19, 2010 on the Takeover Code. A year later, Securities Exchange Board of India ("**SEBI**") has approved the recommendations of TRAC, popularly known as the Achuthan Committee. While most of the TRAC recommendations have been approved by SEBI in entirety, few recommendations have been modified to accommodate the comments provided by the Chambers of Commerce, industry experts and professionals on the TRAC report. It is yet another commendable effort from SEBI to balance legal perfection and the practicalities of India Inc.

While, the complete text of the revised Takeover Code is awaited, the key changes as discussed in the **SEBI board meeting dated July 28, 2011** are highlighted below:

APPROVED RECOMMENDATIONS

- 1. Initial trigger of the Takeover Code:** The first threshold for triggering the Takeover Code, requiring the acquirer to make a mandatory open offer is now increased from 15% to 25% of the voting rights in the target company.
- 2. 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.
- 3. Competitive bid:** In case of multiple competing bidders, the successful bidder can acquire the shares held by the non-successful bidder(s) after the offer period without having to make another open offer. Such acquisition should necessarily be at the same price that was offered by the non-successful bidder(s) to the public.
- 4. Voluntary offers:** Acquirers are permitted to make voluntary offers to the shareholders of the target company subject to fulfillment of certain prescribed conditions.
- 5. Recommendation by the board:** In line with the takeover regulations in other jurisdictions, a recommendation by the board of the target company on the offer made by the acquirer has been made mandatory.

SEBI has accepted the abovementioned recommendations of TRAC without any modifications and the implications of these changes on each of the stakeholders like promoters of the target company, public shareholders of the target company, strategic acquirers and private equity investors are detailed in our earlier hotline, "*Indian Takeover Regulations up for Overhaul!*"

MODIFIED RECOMMENDATION

- 1. Open offer size:** The existing Takeover Code prescribes the minimum size of the mandatory open offer as 20% of the voting capital of the target company. On review of the takeover regulations in other developed jurisdictions, TRAC had recommended that the acquirer should be compelled to make offer for all the remaining shares of the target company. SEBI has clarified that it is not inclined towards accepting the recommendation of the TRAC in this regard in entirety and has increased the offer size from 20% to 26% of the voting capital.

Implications of open offer size on public shareholders

- The recommendation by TRAC to increase the open offer size to all the remaining shares of the target company had generated mixed reactions. The recommendation was perceived as beneficial for the minority shareholders as such an open offer would have assured a complete exit to the public shareholders unlike a proportionate exit in case of the existing open offer for 20% of the voting capital.
- With the open offer size being finalized as 26%, the public shareholders shall not be guaranteed a complete exit even if they tender all the shares in the open offer. Since the acquirer is required to acquire only upto 26% of the voting capital, the public shareholders may get stuck in the target company with part shareholding after the open offer.

IMPLICATIONS ON STRATEGIC ACQUIRERS

- The recommendation of TRAC to increase the offer size to 100% had not gone down too well with the strategic acquirers. Acquisition of all the remaining shares of the target company i.e. open offer of 100% of the voting capital of the target company could turn out to be exceedingly expensive for the acquirers. Especially for the Indian acquirers, this move could have been fatal as funding avenues available to them for financing open offers

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are minimal. Foreign acquirers could resort to leveraged buy outs through bank loans extended by foreign banks but bank loans may not be available to Indian acquirers as Indian banks are not permitted to provide financial assistance for acquisitions.

- Owing to industry pressure, SEBI has now prescribed the offer size as 26% of the voting capital. Though the size of the open offer is increased from 20%, the open offer process is still an affordable affair for the strategic acquirers and this move also creates a level playing field between the Indian acquirers and their foreign counterparts.

- Evidently, SEBI has narrowed down on 26% as the open offer size bearing in mind the initial trigger limit of 25% of the voting capital. The intention is to make any acquirer triggering the takeover code by crossing the initial trigger limit to hold more than 50% of the voting capital of the target company after the open offer subject to the quantum of shares tendered in the open offer. Consequently, such an acquirer would control the affairs and management of the target company.

IMPLICATIONS ON PROMOTERS

- Promoters of Indian companies with staggered shareholding should be mindful of the possibility of a strategic acquirer acquiring shares upto 51% through an open offer under the Takeover Code. This should be highly probable if the promoter shareholding in the target is in the range of 40% to 50% or lesser. The promoters could lose the control of the target company to the strategic acquirer if their shareholding is less than 50% of the voting capital and other shareholders tender their shares to the acquirer.

REJECTED RECOMMENDATION

1. **Delisting: TRAC had recommended that** an acquirer would be required to state upfront in the public announcement, its intention to delist the target company pursuant to the open offer. It was further recommended that if the shareholding of the acquirer is between 75% to 90% after the open offer, the acquirer would be required to either bring his holding down to ensure compliance with the Listing Agreement, or proportionately reduce both his acquisitions under the agreement that triggered the open offer and the acquisitions under the open offer. Also, TRAC had recommended that the acquirer should not be required to make a separate delisting offer under the SEBI (Delisting Of Equity Shares) Regulations, 2009 ("**Delisting Regulations**") if the acquirer exceeds 90% delisting threshold through the open offer under the Takeover Code.

SEBI has indicated that this recommendation of TRAC is rejected. It needs to be seen in the final text of the revised Takeover Code if the recommendation has been rejected in entirety and if the extant provisions on delisting under the Takeover Code are retained.

CONCLUSION

The approval of the TRAC recommendations by SEBI marks the beginning of a new era in the history of India Inc. While TRAC's efforts should be commended in conceptualising the new Takeover Code by incorporating the best takeover practices from developed countries of the world, it remains to be seen how the various stakeholders of India Inc. would react to the revised Takeover Code in the years to come.

- **Arun Scaria & Nishchal Joshipura**

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