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SEBI goes the distance in easing takeover regulations

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Sebi has once again attempted to walk the tightrope not by imposing restrictions, but by encouraging buying on bourses by relaxing the Takeover Code to extend creeping acquisition limit beyond 55%, if done on the floor of the stock exchange.

With stock markets plummeting and most regulators imposing harsh measures like banning short selling, Sebi has once again (after relaxing restrictions on participatory notes) attempted to walk the tightrope for discouraging further selling not by imposing restrictions, but by encouraging buying on bourses by relaxing the Sebi (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (the "Takeover Code") to extend creeping acquisition limit beyond 55%, if done on the floor of the stock exchange.

Sebi recently amended Regulation 11(2) of the Takeover Code to do away with public announcement requirements for consolidation of shareholding through creeping acquisition (including passive acquisition by way of buyback) up to 5% by persons holding 55% and above, but below 75% shares of the target company ("Target"), provided the acquisition is by way of open-market purchases in the normal segment, and not by way of bulk/ block/ negotiated deal, or through preferential allotment and post-acquisition shareholding of the acquirer does not increase beyond 75%.

Prior to the amendments, an acquirer had to make a public announcement for even acquisition of one share if his shareholding in the target was 55% or more. Though this amendment provides leeway to promoters to gain special majority (75% shareholding) over the target, Sebi has however, tried to protect retail investors by subjecting such creeping acquisitions exclusively to open-market purchases.

While Sebi's efforts are indeed commendable, the amendments leave certain scope for confusion and interpretation.

The most critical ambiguity in the amendments perhaps is not to clarify whether the 5% acquisition limit stipulated in Regulation 11(2) is applicable for each financial year, or is only a one-time affair. In fact, on account of the above ambiguity, though a little far-fetched, it is possible to interpret Regulation 11 (2) to imply that a person holding more than 55% shares can go on acquiring shares of the target by open market purchases in less than 5% tranches multiple times in a year.

However, in light of the spirit of the Takeover Code and more particularly Regulation 11(1), it appears likely that the market regulator intended to apply such 5% limit each financial year.

Having said that, there are also views that Sebi probably wants to permit such creeping acquisitions beyond 55% only once in the lifetime of the target, and any further acquisitions whether in the same year, or in the subsequent years should mandate a public announcement. This view is not entirely without foundation as the amendments were introduced as an aggressive measure to bolster the bearish stock market, and it appears likely that Sebi would like to retrogress to a more cautious position as and when the markets gain momentum.

In fact, earlier this year, the finance ministry was contemplating steps to make 25% minimum public shareholding a uniformity across the board for listed companies, but decided against it, apprehending it might encourage further selling activity by promoters and disappoint an already distressed stock market.

Another aspect of the amendments, which encourages debate, is the application of Regulation 11(2) to non-promoters due to buyback, as the amendments obligate even a non-promoter shareholder to make a public announcement for increase in shareholding not intended by him. In fact, the amendments are even more disadvantageous to promoters if their shareholding increases by more than 5% due to an open-market buyback, as they will be required to make a public announcement even when the law prohibits them from participating in such buybacks.

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

The amendments bring to memory the Bajoria–Bombay Dyeing acquisition episode in late 2000, when industrialists, including Ratan Tata, petitioned Sebi to relax the creeping acquisition limit beyond 5% to protect promoters against hostile raiders.

While Sebi has not relented entirely, raising the bar for creeping acquisitions up to 75% will also assist promoters to ward off hostile takeover attempts which are more likely in times like these due to cheap valuations. Sebi has thus walked the tightrope on more than one count, but it ought to take immediate steps to allay the ambiguities highlighted above to help the acquirers and stakeholders interpret the amendments in the manner in which they were intended to by the regulator.

Ruchir Sinha & Nishchal Joshipura

(The authors work for the law firm Nishith Desai Associates)