

M&A Hotline

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SEBI OVERHAULS THE TAKEOVER CODE

Pursuant to its board meeting on September 22, 2009¹, Securities and Exchange Board of India ("SEBI") has sprung into action by bringing out a notification number F.No.LAD-NRO/GN/2009-10/20/182131 dated November 6, 2009 ("Amendment Regulations") to amend the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 ("Takeover Code"). We hereby examine the changes made to the Takeover Code by the Amendment Regulations.

ANALYSIS AND IMPACT OF THE REGULATIONS AMENDED:

Regulation 3(2) – Under the erstwhile Regulation 3(2) of the Takeover Code, acquisition of American Depository Receipts ("ADR") / Global Depository Receipts ("GDR") were exempted from open offer requirement² until the time of their conversion into the underlying equity shares carrying voting rights. SEBI has now clarified that an exemption from open offer would be available only as long as the ADR / GDR holders remain passive investors without any kind of voting arrangement on the underlying equity shares whatsoever. Hence, any customary voting arrangement between the Depository and the ADR / GDR holders providing direct or indirect voting benefits to the ADR / GDR holders could trigger the open offer requirement if such indirect voting right together with direct equity, if any, exceeds the prescribed threshold.

However, the consequence of such an amendment remains unclear in respect to all the existing ADR / GDR issued prior to this amendment. Further, a proviso has been added to Regulation 14(2) of the Takeover Code which provides that public announcement on acquisition of such depository receipts having voting benefits shall be made within four working days of such acquisition.

Regulation 7(1A) – Earlier, an acquirer who acquired shares or voting rights of a company under Regulation 11(1) i.e. equal to or more than 15% but less than 55%, was required to make a disclosure on purchase or sale aggregating two percent or more of the share capital of the target company to the target company and to the stock exchanges.

In addition to the above, with the Amendment Regulations, any acquirer who acquires shares under the terms of Regulation 11(2) i.e. between 55% to 75% or 90%, as the case may be, shall also be required to make disclosure under Regulation 7(1A). This move by SEBI is likely to aim at providing more transparency with respect to public market deals. However, this is not a major shift in the disclosure requirements since such reporting is anyways covered under the disclosure norms of the SEBI (Prohibition of Insider Trading Regulations), 1992.

Regulation 11(1) – By the Amendment Regulations, the much debated ambiguity under Regulation 11(1) has been cleared by SEBI. It has now been clarified that an acquirer (together with persons acting in concert) holding shares between 15% (inclusive) to 55% (under the terms of Regulation 11(1)) can acquire further 5% shares in any given financial year without triggering an open offer (known as 'creeping acquisition') and take its shareholding to a maximum ceiling limit of 55% and not beyond it. For instance, assuming that an acquirer is holding 52% in a target company, the creeping acquisition would be permissible under Regulation 11(1) of the Takeover Code provided that post acquisition, the shareholding / voting rights of the acquirer together with persons acting in concert does not exceed 55% of the equity capital of the target company.

However, under Regulation 11(1), it remains unclear whether the creeping acquisition of 5% in a financial year is to be calculated on a gross basis (only acquisition) or can be netted off against the sales during the financial year. However, in a recent circular dated August 6, 2009 issued by SEBI, it was provided that under Regulation 11(2) the spirit and intention is to cover and allow the 5% margin on gross basis and it may be prudent to adopt the same practice for Regulation 11(1).

Second proviso to Regulation 11(2) – It has been clarified that the creeping acquisition of 5% allowed under the terms of second proviso to Regulation 11(2) i.e. between 55% to 75% would be allowed to the acquirer irrespective of the earlier acquisition made under Regulation 10 or Regulation 11(1) of the Takeover Code.

This raises an interesting question – whether an acquirer can acquire 5% shares under Regulation 11(1) and subsequently take shelter of Regulation 11(2) to acquire further 5% shares in the same financial year?

CONCLUSION

With quite a few ambiguities prevailing in the Takeover Code, its provisions became prone to several interpretations; leading to several non-compliances and penalties. Having wide implications, the changes made by SEBI under the Amendment Regulations have cleared a few loose ends under the Takeover Code. With the special committee constituted for review of the Takeover Code and it being open to suggestions from the public at large, SEBI may

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follow more simplified regulations in the times to come.

- Sambhav Ranka, Vaidhyanadhan Iyer & Siddharth Shah

(M&A Practice Group Members)

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