

Distorted reform in takeover law

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Finally, the Securities and Exchange Board of India (“SEBI”) is doing it – the heavily bandaged and plastered takeover regulations, which have been crying for a review, are being replaced. However, SEBI’s board has shied away from fundamental systematic reform.

The takeover regulations are badly in need of repair. Drafted in 1997, they have conceptually served the capital market well, but serious conceptual ambiguity and drafting lacunae have plagued the regulations. Last July, the Takeover Regulations Advisory Committee (“TRAC”) submitted an entire new scheme of the regulations in a bid to make them commensurate with India’s position as the fourth largest economy of the world (in terms of purchasing power parity). The prime recommendation of the TRAC was an obligation to require an acquirer to offer the purchase of any share that any other shareholder desired to sell (popularly mis-named as the “100% offer size”) instead of offering to acquire a mere 20%.

On the back of this core and foundational reform, other measures such as shoring up the trigger level for a mandatory open offer from a voting power of 15% to 25%, and continuing to permit “creeping acquisitions”, were recommended. Expectedly, fundamental reform is not easy to carry through, and the most important measure viz. imposing an obligation to acquire every share tendered by shareholders has been given up. Yet, the leeway on the triggering threshold and the continuance of creeping acquisitions, have been ushered in.

Even in 1997, when the takeover regulations were first drafted, an advisory committee that then made recommendations had a sole dissenting voice in favour of this measure (it was not a jholawalla socialist, but reputed investment banker Nimesh Kampani). Essentially, the concept of requiring a substantial acquirer to make an offer to acquire all the shares from the remaining shareholders is driven by the acknowledgement that when a substantial change in shareholding of a listed company occurs, the other shareholders have a right to exit. Such shareholders ought to have the ability to sell whatever they choose to sell rather than have to queue up before a rationing system where their shares would only be proportionately acquired while a substantial shareholder could sell all his shares to the incoming acquirer.

Sections of society that prefer to remain backward in thinking were up in arms. They have successfully killed this measure of reform. The other reforms such as the hike in the triggering threshold and the continued availability of “creeping acquisitions” have found their way in, without adopting the basic reform on how an open offer is to be made. The token offer size of 20% has been replaced by another token offer size of 26%. In 1997, creeping acquisitions i.e. acquisitions to further consolidate holdings and improving the degree of control without making an open offer, as a temporary measure to help those controlling our listed corporate world to cope with living the life of a truly listed company. That measure is now permanent.

Another reform measure that is necessary to help acquirers of listed companies take such companies private in an equitable, transparent and fair manner, has also been killed. When one acquires a substantial stake in listed companies and complies with a mandatory requirement to make an open offer, one could end up with a shareholding in excess of 90%. In such a situation, the TRAC proposed that the company could be delisted since such a vast majority would anyway have opted for letting the company get delisted. A corollary of this measure was a proposal to enable an acquirer to acquire shares under the

takeover regulations in a proportionate manner i.e. pare down what is acquired from the seller of substantial shareholding and the public shareholders selling under the open offer, to remain listed. This entire framework, which was essentially a means of enabling a simple and fair manner of reconciling continuous listing requirements, with the takeover regulations has been rejected.

The TRAC painted a portrait to present a dynamic portrait of the face of M&A in India. The changes to the recommendations are like elongating the nose to suit one viewer's taste, and shortening the neck to suit another viewer's taste, leaving the circumference of the face intact.

The distorted final picture is not what the TRAC envisaged. Perhaps sticking to a drafting clean-up would have sufficed.

Disclosure: The author was a member of the TRAC. (The author is a partner of JSA, Advocates & Solicitors. The views expressed herein are his own.)

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