# Recoding takeovers: Examining the changes

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Few pieces of legislation have made as immediate and wide-sweeping an impact as the Takeover Code did when it was first introduced in 1997. It was a milestone marking the beginning of India's corporate growth and consolidation story. Thirteen years on, the country's M&A space has grown from a gawky adolescent to a feisty young adult.

To keep pace with market realities and demands, the Securities & Exchange Board of India (SEBI), the capital market regulator, has initiated a rethink of the Takeover Code. It entrusted the task of articulating what needs to be done to the Takeover Regulations Advisory Committee (TRAC), which comprises a range of industry experts. SEBI has recently made TRAC's recommendations public and has invited feedback on them. The committee has advocated some bold, fundamental changes and we discuss the highlights below.

## Raising the thresholds

Under the current code, an acquirer is required to make a mandatory open offer to provide other shareholders an exit upon hitting the 15% threshold. This was believed to give the acquirer substantial control in the Indian context where listed companies generally had low promoter shareholdings. This is no longer the case and average promoter holdings in India have seen a steep jump since the open offer benchmarks were first set.

Acknowledging that 15% control may often not constitute a threat to existing promoters, TRAC has suggested that an open offer be triggered only when an acquirer is in control of 25% of the target. This is in line with global trends – jurisdictions like the UK, Singapore and Hong Kong, which have more sophisticated markets, peg the threshold at 30-35%. Moreover, a 25% stake gives a shareholder negative control by allowing it to effectively block special resolutions, making this a more appropriate trigger point. The proposal bodes well for financial investors who will have the option of taking bigger punts on their chosen targets without going through the expensive and cumbersome open offer process.

## No second open offer

The other big change proposed is to do away with the requirement to make a second open offer when a 55% stake in the target is acquired. Under the present regime, acquisition of up to 5% per year is permitted without an open offer being triggered till the 55% mark. TRAC has suggested that this be relaxed and the acquirer be allowed to inch up all the way till 75% by creeping acquisition on an annual basis. This is the maximum permitted and a company would be required to delist if public shareholding falls below 25%.

Based on its market research, TRAC concluded that the trend in most Indian listed companies is for promoters to wield control with less than a 50% shareholding. In fact this often yields a higher effective voting right, as retail shareholders do not always turn up for general meetings and the fate of a resolution is determined based on the will of a majority of the shareholders actually present. In light of this, the 55% trigger is rendered somewhat ineffective as the battle for control is likely to be fought at a lower shareholding threshold.

## Open offer

The most significant shift proposed by TRAC relates to the quantum of shares that an acquirer is required to purchase as part of an open offer process. The current minimum is 20%, but TRAC believes that open offers should provide an exit option to all shareholders for their entire holding. Accordingly, a requirement to pick up 100% has been mooted.

This ties in with the proposed abolishment of the 55% trigger – the logic being that when the acquirer attains negative control at 25%, all the other shareholders should get an option to exit in their entirety. If the shareholder chooses to stay with the acquirer at this stage, the acquirer should not be required to give the shareholder a second exit on reaching 55%, given the costs involved in making such an offer. While this single window may improve efficiency to some extent, there is some concern that transaction costs involved in making an open offer for 100% may become prohibitive and slow down takeover activity in India.

## Equal fees

The Takeover Code permits acquirers to pay selling promoters or significant stakeholders of the target a non-compete fee over and above the offer price, provided such payments do not exceed 25% of the offer price. TRAC believes that discriminating between shareholders is inappropriate and has recommended that all shareholders receive the same price. This is intended to protect the interests of retail and other shareholders with less bargaining power.

While these recommendations have sparked much heated debate, the general consensus is that an overhaul of the Indian Takeover Code is in order. The hope is that the government will take on board suggestions from the public as well and make a decision on the matter sooner rather than later.

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