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CORPORATE RESTRUCTURING: UNDERSTANDING THE CONCEPT OF ACQUISITION AND TAKEOVER

By Shreya Somani
From Jindal Global Law School, OP Jindal Global University

Abstract

In this Paper an attempt has been made to understand what acquisition is, what is difference between acquisition and takeover, the regulatory framework surrounding acquisition and takeovers. What is the difference between the process of acquisition that has been given under section 236 of the Companies Act, 2013 and that under the SEBI Takeover Code. This paper also seeks to explore the trends and progress in Takeovers and acquisition In India.

Key words: Corporate Restructuring, Acquisition, Takeover, Differences

Introduction

Businesses in modern economies are vastly different from that in past decades. Modern economies are defined as a highly dynamic, quickly changing, and competitive environment where business strategies are frequently put to the ultimate test. The rising worldwide market competitiveness has forced Indian businesses to consider corporate restructuring as a crucial strategic option. Corporate restructuring refers to a decision made by the corporate entity to radically alter its capital structure or activities. Corporate restructuring often takes place when an organisation is facing severe problems and is at risk of going insolvent. In today's modern corporate world, the mergers, acquisitions, and takeovers process has grown considerably in value. This method is frequently used to restructure corporate entities.

Two of the corporate world's most frequently misunderstood terms are mergers and acquisitions. Usually people use the words mergers, acquisitions, and takeover interchangeably, however each have different meanings. When two independent companies join forces to form a single, new company, a merger takes place. An acquisition, on the other hand, is the taking over of one company by another. Although the words "acquisition" and "takeover" are frequently used interchangeably, they each have a somewhat distinct meaning. Acquisition refers to the act of one company purchasing another with the consent of the board of directors of that other company. While a takeover refers to the acquisition of control of an already-registered firm through the sale or exchange of shares. In order to obtain control of a company, a takeover often entails the acquisition or purchase of its owners' shares at a predetermined price up to the point of at least majority ownership. A takeover is a distinctive kind of acquisition that happens when one firm takes control of another without the consent of the acquired company. This is the main distinction between an acquisition and a takeover. When shares are bought with the goal of taking over the target company, the transaction is known as a takeover.

In India, the takeover and acquisitions our governed by the Companies Act 2013 and also by SEBI Regulations. Section 230 to 240 of the Companies Act, 2013 cover the statutory provisions governing M&As.[1] Specifically, referring to the acquisition process described in Section 236 of the 2013 Companies Act,[2] which introduces the concept of "squeeze out." Squeeze out alludes to the majority shareholders' purchase of minority shareholders by monetary compensation. Through this process, the shareholders who control 90% or more of the stock in a corporation have the authority to buy out the minority shareholders' shares. It serves as a technique to minimize the influence of minority shareholders. In 2011, the enactment of new Takeover Regulations brought significant regulatory changes to the takeover and acquisition trend in India.[3] In particular, new regulation was enacted to govern Public listed companies. In this Paper an attempt has been made to understand the difference between the process of acquisition that has been given under section 236 of the Companies Act, 2013 and that under the SEBI Takeover Code 2011.

Corporate Restructuring

The process of redesigning one or more aspects of a company is known as corporate restructuring. The process of reorganizing a company may be implemented for a variety of reasons, including positioning the company to be more competitive, surviving a currently adverse economic climate, or acting on the corporation's self-confidence to move in an entirely new direction. Before restructuring, there must be an existing structure that may have many limitations/restrictions such as finance, legal, business, and management that must be considered. In other words, restructuring could be defined as making some changes to the existing structure. The process of corporate restructuring is regarded as critical in order to eliminate all financial crises and improve the company's performance. Corporate restructuring is a comprehensive process that allows a company to consolidate its business operations and strengthen its position in order to achieve both short-term and long-term corporate goals. Corporate restructuring is critical for a company's survival in a competitive environment. The concept of restructuring entails adopting new ways of conducting business and abandoning old ones. It necessitates that organizations constantly reconsider their organizational design and structure, organizational systems and procedures, formal statements on organizational philosophy, and values, leader norms and reactions to critical incidents, as well as criteria for rewarding, recruiting, selecting, promoting, and transferring employees. A company that has been effectively restructured will be leaner, more efficient, better organized, and more focused on its core business.

The following are different types of Corporate Restructuring:

- Merger
- Demerger
- Reverse Merger
- Disinvestment
- Takeovers
- Joint Venture
- Strategic alliance
- Franchising
- Slump Sale

[1] The Companies Act, 2013 § 230-240.
[2] The Companies Act, 2013, § 236.
[3] SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

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A Look at Acquisition

A company makes an acquisition when it buys the majority or all of the shares of another company in order to take over that business. Acquisitions may be made by subscribing to newly issued shares by the target company or by purchasing existing shares of the target company. In most cases, acquisitions are conducted in order to manage, enhance, and seize synergies from the target company's strengths.

Although in theory the terms "acquisition" and "takeover" have nearly identical meanings, but practically they have different connotations. In general, "acquisition" describes a primarily amicable transaction, where both firms cooperate; "takeover" suggests that the target company resists or strongly opposes the purchase; another term Merger which is also usually confused with acquisition; the term "merger" is used when the purchasing and target companies mutually combine to form a completely new entity.

Difference between mergers, acquisitions, takeover

Mergers:

A merger is a more-than-friendly acquisition because it is the mutual fusion of two companies into one new legal entity. Mergers typically take place between companies that are roughly comparable in terms of basic characteristics such as size, number of customers, scale of operations, and so on. The merging companies are convinced that their combined entity will be more valuable to all parties (particularly shareholders) than either would be separately.

Acquisitions:

Friendly acquisitions occur when the target company agrees to be acquired and its board of directors (or board) approves the acquisition. Friendly acquisitions frequently benefit both the acquiring and target companies. Both companies devise strategies to ensure that the acquiring company acquires the appropriate assets, and they examine the financial statements and other valuations for any obligations that may be associated with the assets. The purchase is completed once both parties have agreed to the terms and have met any legal requirements.

Takeover:

Unfriendly acquisitions, also known as "hostile takeovers," happen when the target company refuses to accept the acquisition. Because the target firm does not have the same agreement in hostile acquisitions, the acquiring firm must actively purchase large stakes in the target company to gain a controlling interest, which forces the acquisition.

Even if the takeover is not hostile, it implies that the companies are not equal in one or more significant ways.

Regulatory Framework of Acquisition

The Indian corporate sector is multi-sectoral and regulated by multiple regulatory bodies. The Indian Companies Act, 2013 (the "Companies Act") is the primary piece of Indian legislation governing the establishment and operation of businesses in India. It contains laws (sections 235 and 236) as well as guidelines for acquisitions. The Securities and Exchange Board of India, governs corporate activities in addition to the Companies Act. Companies are also governed differently depending on whether they are public or private. The SEBI has made Securities and Exchange Board Of India (Substantial Acquisition Of Shares And Takeovers) Regulations, 2011. These regulations shall apply to direct and indirect acquisition of shares or voting rights in, or control over target company

Acquisition under Companies Act 2013

Acquisitions can be made by purchasing existing shares of the target or subscribing to new shares issued by the target.

i. **Transferability of shares:** The articles of association may prescribe certain procedures for the transfer of shares that must be adhered to in order to affect a transfer of shares. It is therefore prudent for a buyer of private company shares to ensure that the non-selling shareholders (if any) waive their pre-emption rights and any other preferential rights that they may have under the articles of association. Any transfer of shares, whether of a private or public company, must follow the procedure specified in the articles of association.
ii. **Squeeze Out Provisions- Section 236 of CA 2013:** Section 236 of CA 2013 states that if a person or group of people acquires 90% or more of a company's shares through an amalgamation, share exchange, security conversion, or other means, such person(s) shall, in addition to notifying the company of their intention to buy the remaining equity shares of the company, have the right to make an offer to buy out the minority shareholders at a price determined by a registered valuer.[4]

Analysis of Acquisition Under Section 236 of Companies Act, 2013 "Squeeze out Provision"

Background

Typically, the majority shareholders own more than 50% of the company's shares, while minority shareholders own less than 50% of the company's shares. However, under Section 236 of the Act, 'minority shareholding' refers to shareholders holding no more than 10% of the company's shares. So, technically, the majority shareholders have a significant influence on the company's decision-making process. Section 236 of the Companies Act, 2013 establishes a process for squeezing out minority shareholders in which any shareholder of the company, acting alone or in concert, holding 90% or more of the total issued equity share capital, may acquire the company's remaining equity shares by making an offer to the minority shareholders.[5]

In Foss v. Harbottle[6], the concept of "majority rule" was born. In the case, the two minority shareholders of Victoria Park Company filed a lawsuit against the company's five directors, alleging that the company's property was misused and misapplied, and that mortgages on the property were improperly granted. They asked for the appointment of a receiver. The Court ruled that the plaintiffs lacked the necessary legal standing to bring such proceedings against the company or its representatives. Furthermore, the court ruled that minority shareholders are bound by the majority shareholders' decision. As a result, the 'Majority Rule' was established.

[4] The Companies Act, 2013, § 236.
[5] Ibid
[6] Foss v Harbottle, (1843), 2 Hare 461, 67 ER 189.

The law on minority squeeze-out has not been a glorious chapter in India's company law history. As a matter of legislative policy, the Parliament appears to be hesitant to pass legislation requiring minority shareholders to sell their shares. The government sees it as a form of 'expropriation.' As a result, despite the specific recommendation of the Dr. JJ Irani Committee[7], our Parliament has taken a conservative approach while providing majority shareholders with the mechanism to 'buyout' minority shareholders' shares.

Scheme of section

Section 236(1) of the Act states that if an acquirer, or a person acting in concert with such acquirer, becomes a registered holder of 90% or more of a company's issued equity share capital, or if any person or group of persons becomes 90% majority or holds 90% of a company's issued equity share capital, because of an amalgamation, share exchange, security conversion, or any other reason, such acquirer, person, or group of persons, as the case may be, shall notify the company of their intention to purchase the remaining equity shares.[8]

Section 236(2) states that the acquirer/person/group of persons described in Section 236(1) must make an offer to the company's minority shareholders to buy the equity shares held by such shareholders at a price determined by a registered valuer in accordance with such rules as may be prescribed.

Section 236(3) states that, subject to the provisions of Sections 236(1) and 236(2), the minority shareholders of the company may make an offer to the majority shareholders to purchase the company's minority equity shareholding at a price determined in accordance with the rules prescribed in Section 236. (2).[9]

Sections 236(4) to 236(9) [10]specify additional compliance requirements that must be met after the majority shareholder(s) exercise the rights granted by Sections 236(1) and 236(2). (2). The method for determining the fair value of shares in both listed and unlisted companies is outlined in Rule 27 of the Companies (Compromises, Arrangements, and Amalgamations) Rules, 2016.[11]

It is also worth noting that valuation for the purposes of Section 236(2) should be performed by a registered valuer in accordance with Section 247 of the Act and the Companies (Registered Valuers and Valuation) Rules, 2017.

The decision of the NCLAT in S. Gopakumar Nair v. OBO Bettermann India Private Limited [12]is instructive in determining the scope of Sections 236(1) and 236(2).

In OBO Bettermann, the majority shareholders (who held 99.64% of the company's shareholding) attempted to compulsorily acquire the minority shareholders' shares by issuing notices under Section 236.

The NCLAT ruled that the majority shareholder(s) can invoke Section 236 only if

[7] Report of the Expert Committee on Company Law, chaired by Dr. Jamshed J. Irani, submitted to the MCA on May 31, 2005.
[8] The Companies Act, 2013, § 236 (1).
[9] The Companies Act, 2013, § 236 (2).
[10] The Companies Act, 2013, § 236 (4) (9).
[11] *The Companies (Compromises, Arrangements, and Amalgamations) Rules*, 2016, Rule 27.
[12] S. Gopakumar Nair v. OBO Bettermann India Private Limited Company Appeal (AT) No. 272/2018.

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either of the 'events' specified in Section 236(1) have occurred, implying that the majority shareholder must hold or acquire a minimum of 90% of the shareholding "by virtue of an amalgamation, share exchange, conversion of securities, or for any other reason." It was held that the words "for any other reason" should be read ejusdem generis with the preceding words and would only include "events" similar to a merger, share exchange, or security conversion.

The NCLAT also noted that, whereas Section 235 deals with the acquisition of shares from dissenting shareholders in specific circumstances, Section 236 deals with the acquisition of shares from assenting shareholders if either of the 'events' specified in Section 236(1) has occurred.

Analysis of Takeover code 2011

On a case-by-case basis, the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 defined the term Acquisition. SEBI has newly defined "acquisition" as "directly or indirectly acquiring or agreeing to acquire shares or voting rights in, or control over, a target company" in Regulation 2(1)(b) of the Takeover Code[13]. Furthermore, the Takeover Code defines a "acquirer" as any person who, directly or indirectly, acquires or agrees to acquire shares or voting rights in, or control over, a target company, whether by himself, or through, or with persons acting in concert with him. The definition of "acquirer" under the 1997 Code has been retained in the Takeover Code, with a few literal changes. The term acquisition is widely used in the Takeover Code; defining it gives it a consistent meaning throughout the Code. Direct acquisitions and indirect acquisitions are the two types of acquisitions. The acquirer is subject to different obligations under the Takeover Code depending on whether the 'acquisition' is direct or indirect. Control of a publicly traded company is acquired directly by acquiring shares of the target company, whereas indirect acquisition is accomplished by acquiring shares of the target company's holding company/parent company.

The Takeover Code requires an open offer process for both direct and indirect acquisitions of shares, voting rights, or control if such acquisitions exceed the Takeover Code's threshold.

Acquisition of Control

The acquisition of control differs significantly from the acquisition of shares and voting power. Regulation 6 of the Takeover Code requires a public announcement of an open offer to acquire control of a target company, either directly or indirectly. This is regardless of whether a target company's shares or voting rights are acquired or held. [14]

Indirect Acquisitions of Share or Control

Regulation 5 of the Takeover Code 2011[15] recognises the concept of indirect share acquisition. It defines indirect acquisition as the acquisition of shares, voting rights, or control over any other company that would allow the acquirer of such shares, voting rights, or control to exercise such percentage of voting rights that would otherwise have triggered an open offer process, allowing the acquirer to exercise control over a company. Certain indirect acquisitions are considered

[13] Takeover code, 2011, n 3, Regulation 2 (1)(b).
[14] Takeover Code, 2011, n3, Regulation 6.
[15] Takeover Code, 2011, n3, Regulation 5.

'deemed direct acquisitions' if the following conditions are met, such as:

a) the target company's proportionate net asset value as a percentage of the consolidated net asset value of the entity or business being acquired exceeds 80%; or
b) the target company's proportionate sales turnover as a percentage of the consolidated sales turnover of the entity or business being acquired exceeds 80%; or
c) the target company's proportionate market capitalisation as a percentage of the enterprise value of the entity or business being acquired exceeds 80%; the 'deemed direct acquisition' must adhere to the same mandatory open offer requirements as a direct acquisition of shares, voting rights, or control.

Voluntary Offer

Regulation 6 allows shareholders who already own at least 25% but less than 75% of a company's shares or voting rights to make a voluntary offer under the Takeover Code 2011 to further consolidate their existing shareholding in the company.[16] This is a one-of-a-kind option not available under the Takeover Code of 1997. The voluntary offer allows such shareholders to acquire additional shares representing at least 10% of the company's total shareholding. However, this flexibility is not provided to shareholders without conditions, such as:

i. a person who (together with PACs[17]) has acquired shares or voting rights in the preceding 52 weeks other than through an open offer is ineligible to make a voluntary offer;
ii. acquisition of any shares in the target company is prohibited during the offer period of such voluntary offer;
iii. the acquirer who makes a voluntary offer is ineligible to acquire any shares of the target company for a period of six months after the completion of that voluntary offer; and
iv. if the offer is accepted in full, the number of shares proposed to be acquired under the voluntary offer should not be such that it reduces the target company's public shareholding below the minimum permissible limit.

Difference Between Acquisition Under Takeover Code and Section 236 of the Companies Act 2013

Both section 236 of the Companies Act and the takeover code's requirements refer to the majority's purchase of shares, however there is a little distinction between the two. The Takeover Code's rules expressly apply to listed corporations, although the Companies Act makes no such mention. A public offer is made to the company's shareholders in accordance with the takeover code. If there is a significant change in the ownership pattern as envisioned in the Code or if the Target Company changes hands, it refers to the exit option provided to the public to reduce their shareholding in the Target Company.

The shares of publicly traded firms must adhere precisely to the rules outlined in the code in order to avoid having their shares delisted. Investor protection from the damaging consequences, particularly hostile takeovers. There is no provision in Section 236 that would cause the firm to be delisted if it were not followed correctly. Moreover,

[16] Takeover Code 2011, n 3, Regulation 6.

[17] Takeover Code 2011, n 3, 2(1)(q)(2).

the chances of Hostile takeover under section 236 is more.

The following is ensured by the Code:

- Give investors a chance to leave if they don't want to remain with the new management,
- the open offer's full and accurate disclosure of all relevant information to enable investors to make an educated selection,
- ensuring that the promoters have the financial resources to pay the acquisition price to the investors,
- completion of takeover procedures on time.

Minority shareholders are not adequately protected under section 236. The Act is also ambiguous on how long minority shareholders must give up their interests to majority owners before doing so. Since the Act makes no mention of holding a separate meeting for minority shareholders to address their concerns with the majority shareholders' purchase of their shares, therefore there is no exit opportunity given to dissenting shareholders.

Trends and Progress

There have been many cases of acquisition in India. Specifically talking about hostile takeover cases in India there have been made various attempts but only two of these attempts, nevertheless, led to the transfer of ownership. The case of India Cements takeover Rassi Cement is one of the classic examples of a hostile takeover ultimate acquisition of the target by a hostile bidder occurred in 1998 when BV Raju sold his 32% stake in Raasi Cements to India Cements.

L&T and Mindtree [18]acquisition was the second successful hostile takeover. Larsen and Toubro Ltd (L&T) gained a controlling interest in Mindtree Ltd, raising its stake to 60% in the Bengaluru-based company in 2019.

L&T completed buying the 31% additional stake it targeted to acquire in Mindtree for ₹4,988.82 crore through an open offer as large investors rushed to sell their holdings. The 60% stake in Mindtree gives L&T complete control over the software company's board and management. The purchase of additional shares through an open offer by L&T after acquiring a 20.4% stake in Mindtree from coffee baron VG Siddhartha and affiliate firms marked the culmination of a year-long effort by the Mumbai-based engineering giant to gain control of Mindtree through a hostile bid.

Recently, a battle to control the management of New Delhi Television Ltd. (NDTV), which operates one of the leading television news outlets in the country, is brewing between the Adani Group and the founders of NDTV. In accordance with SEBI regulations, the Adani Group launched an open offer to purchase 26% of the public shareholders' shares for Rs. 294 per share, a total cost of 483 crore, after exercising the option to convert the warrants into equity stakes.

18 Anirudh Laskar, *With 60% stake, L&T completes its hostile takeover of Mindtree*, 27 June 2019, https://www.livemint.com/companies/news/with-60-stake-l-t-completes-its-hostile-takeover-of-mindtree-1561536743325.html

How Adani acquired stakes in NDTV[19]

- In 2009, Vishwapradhan Commercial Pvt. Ltd. (VCPL) received convertible warrants from RRPR Holdings, which is controlled by NDTV founders Prannoy Roy and Radhika Roy, in exchange for a loan from the latter. These warrants had a conversion value of 99.99% of RRPR equity shares, which had a 29% holding in NDTV, when converted.
- The Roys appeared eager to issue such a warrant because they had to refinance debts they had borrowed from the ICICI Bank, which had a 19% annual interest rate.
- As a type of dramatic intervention, a company named VCPL, sponsored by the Reliance group, gave RRPR a loan with no interest.
- As a result, the agreements between RRPR and VCPL included convertible warrants, call options on NDTV shares granted to VCPL's associates, and rights like the ability to appoint directors to RRPR and the requirement to obtain VCPL's prior written consent before raising money, establishing a subsidiary, buying back shares, selling RRPR's shares in NDTV, among other things.
- AMG Media Networks Limited, owned by The Adani Group company, which recently acquired VCPL, immediately exercised the option to convert the warrants into shares of RRPR. Additionally, this resulted in an open offer under the Takeover Code.

Conclusion

The Takeover code 2011 aimed to balance the interests of shareholders and promoters, is reflected in the takeover law of 2011. The Code offers a number of distinctive features not found in the previous Code as well as Section 236 of the Companies Act, including opportunities for public shareholders to exit, a rise in the minimum share size required to make an open offer from 15% to 25%, indirect acquisition, a revised list of exemptions, and many more. The shares of public listed company must closely adhere to the rules outlined in the code in order to avoid having their shares delisted. To safeguard investors from the negative consequences that takeovers, particularly hostile takeovers, may have on their interests, such rigorous adherence to the rules is required. The Takeover Code 2011 places a strong emphasis on the ideas of corporate democracy, transparency, justice, and protecting investors' interests.

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