Sebi Changes Code to Ease Takeovers by India Inc

Trigger for open offer raised to 25% from 15%; size of offer increased to 26% from 20%

UK SINHA'S
Maiden Innings

TAKEOVER CODE

MEASURE
Open offer trigger limit raised from 15% to 25%

IMPACT
More M&As, board battles. Action likely in stocks like LeelaVentures (ITC 14.8%) & EIH (RIL & ITC hold 15% each)

MEASURE
Acquirer to make open offer for 26% instead of 20% currently

IMPACT
Will make M&As more expensive, but is unlikely to hinder such transactions

MUTUAL FUNDS

MEASURE
MFs can collect, as one-time fee, ₹100 for existing folios & ₹150 for new folios

IMPACT
Entry load may return in a softer avatar, but not impact investors much. More incentive for agents to sell SIPs

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The Securities & Exchange Board of India, or Sebi, has proposed new takeover rules that will ease acquisitions by Indian companies and scrap the non-compete fee, an anomaly that enriched promoters over minority shareholders. But it will dilute the spirit of a committee that mandated total buyout of minority holders by acquirers as in the developed markets.

The minimum holding requirement to trigger an offer to minority holders has been raised to 25% of the company from 15%. Once that level is reached, the acquirer must offer to buy 26%, up from 20% now.

New norms make it mandatory for the board of the target company to suggest its opinion to shareholders, and the rise in minimum limit may benefit private equity investors who can own more of a listed company without having to invest a substantial sum.

"Going by our interactions with people who matter in the banking regulatory circles, it was understood that bank financing of acquisitions may not happen in the near future," Sebi Chairman UK Sinha told reporters after a board meeting. "We should not start something that will only help a certain set of investors," he said referring to international companies that get liberal funding from their banking systems.

A committee headed by C Achuthan, after many complaints that minority holders were shortchanged during takeovers, had proposed that the acquirer offer to buy out all the minority holders, which could lead to delisting of a stock from the exchanges, so that the benefit of a takeover is uniform. But corporates and investment bankers said it would raise the cost of acquisition in a country where banks are barred from funding takeovers. Achuthan, a former presiding officer at the Securities Appellate Tribunal who ruled on many takeover disputes, was also for scrapping the non-compete fee.

Sebi also abolishes non-compete fees usually paid by buyers to sellers in M&A deals

Ever since the Achuthan committee submitted its report, corporates and investment banks have been against some of the proposals such as 100% buyout.

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Under New Rules Any Takeover can Lead to 51% Ownership

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The report also recommended scrapping of the so-called 'non-compete fee' that many promoters took advantage to benefit more than other shareholders.

"The move to increase the threshold limit to 25% will increase private equity activity," said V Anantharaman, regional co-head, wholesale banking, South Asia, Standard Chartered Bank. "And the move to increase the open offer size to 26% will ensure the transaction in which control is sought, the objective of the acquirer is met. It would have been good if certain changes in delisting guidelines were also implemented to make it more practical."

Mergers and acquisitions in India fell 37% to $27.5 billion last year, data from Bloomberg shows. The proposed norm for buyout of minority holders differs from what is in practice in developed markets. Regulations in Japan, Hong Kong and Singapore mandate total buyout of minority holders.

The new norms also indicate the regulator is particular that those who manage the company rather take controlling stake than doing with smaller stakes.

"The amendments also suggest the regulator's underlying intention appears to be that once an acquirer takes 25%, there must be a definite change in the management control," said Vishwang Desai, managing partner, Desai & Diwanji, a leading M&A law firm that ranked No. 1 on the M&A tables for 2011 prepared by Mergermarket.

"Previously, with 15% threshold and 20% offer size limit, there were situations where control could still continue with the previous management."

Now, any takeover could lead to 51% ownership.

Although all minority holders won't benefit to the fullest of their holdings, it may be something better than the previous one. "For minority shareholders, the increase of open offer size to 26% is a positive move because it results in higher acceptance ratio from public shareholders," said Mehul Savla, director at RippleWave Equity Advisors. "But, for promoters, it could create an imbalance. For those promoters having a low holding in the company, they continue to have a restriction of 5% (creeping acquisition) whereas a minority investor can acquire up to 25% without any time limit for making an open offer."