SUBSTANCE OVER FORM IN INDIA'S OPEN OFFER REGIME

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ABSTRACT

India's open offer regime, set out under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, was designed to give public shareholders a fair exit whenever control of a listed company changes hands. This piece looks at how the rule actually plays out in practice, not just on paper. It walks through when an open offer kicks in, how courts have read the idea of "control," and what happens when control shifts through indirect routes like inter-corporate loans or court-approved schemes, where the usual triggers don't apply in an obvious way.

The Adani-NDTV deal is used as a working example. The takeover went through every formal SEBI requirement and the price followed the prescribed formula, yet NDTV's founders walked away with a far better price than the open offer gave ordinary shareholders. Nothing here was unlawful, but it exposes the real gap between following the rules and actually treating minority shareholders fairly.

The broader argument is that the regime has done real good. It has made acquisitions more predictable and given minority shareholders a way out when control changes. But ticking the procedural boxes doesn't always mean shareholders get a fair deal, especially in indirect or privately structured acquisitions. The piece argues that regulators and courts need to keep looking past form and into substance, while being careful not to over-regulate in a way that scares off legitimate deals.

Introduction

The control of a company is usually transferred that affects the interests of its public shareholders particularly when a listed company is involved in a merger or acquisition. Acquisitions and takeovers can improve both the operational effectiveness and the value to shareholders but concerns certainly arise about the interests of minority shareholders who usually have little or no say in acquisition-related decisions.

In order to address the mentioned concerns, the Securities and Exchange Board of India introduced SEBI (Substantial Acquisition of Shares and Takeovers) Regulations 2011, which require any purchaser acquiring a specific threshold number of shares or gaining control over a company to make an open offer to the public shareholders prior to closing on the acquisition.

Contemporary M&A transactions have prompted examination of whether procedural compliance with the takeover code consistently achieves its stated objectives. This blog will investigate the legal structure governing open offer commitments, examine how the courts have interpreted the safeguards for minority shareholders, and evaluate the effectiveness of the regime in contemporary Indian M&A transactions.

Open Offer Obligations Under the Sebi Takeover Code

The mandatory open offers in the acquisitions of listed companies are governed by the ***SEBI (Substantial Acquisition of Shares & Takeovers) Regulations, 2011*** i.e. ***the Takeover Code***

It mentions conditions that must be fulfilled for the acquirer to be obliged to carry out a mandatory offer to the public shareholders with primary focus on the respective thresholds.

Under ***Regulation 3(1)*** of the Takeover Code, "the obligation to make an open offer arises upon acquisition of 25% or more of the voting rights in a listed company listed on the stock exchange". Notwithstanding any need to meet a shareholding threshold, ***Regulation 4*** requires an acquirer to make an open offer after 'acquiring control' as defined in Takeover ***Regulation 2(1)(e)***. The concept of control comprises of the right to appoint a majority of the board of directors or to influence the administration or policy of the company either directly or indirectly. The Takeover Code also permits limited incremental acquisitions through the mechanism of creeping acquisition. Under ***Regulation 11***, an acquirer holding voting rights between 25% and 75% may acquire up to 5% of the shares in a financial year without activating an open offer.

Certain transactions are exempted from open offer obligations under ***Regulation 10*** which includes the acquisitions pursuant to court or the tribunal-approved schemes of arrangement. These schemes are mentioned in ***Section 230 to 232 of the Companies Act, 2013*** but their relevance to takeover regulation is determined by the exemption framework mentioned under the Takeover Code. At the same time, judicial and regulatory interpretation is required in order to ensure consistency with the objectives of takeover regulation.

From a regulatory perspective, the open offer mechanism provides opportunities for public shareholders in control transactions. The Supreme Court in the case ***Nirma Industries Ltd. vs. Securities and Exchange Board of India*** described the Takeover Code as a beneficial legislation thereby emphasizing that its provisions must be interpreted with respect to their investor protection objective rather than by an altogether technical implementation.

The Judicial Interpretation and Practical Challenges

Although the SEBI Takeover Code has laid down some specific thresholds to trigger the obligation to make an open offer, its application has certainly raised interpretative issues particularly in the context of an acquisition of control. Judicial interpretation indicates that takeover regulations are assessed in light of their underlying objectives. A central issue in judicial interpretation concerns the concept of 'control' under the Takeover Code. In ***Subhkam Ventures (I) Pvt. Ltd. vs. SEBI***, the Securities Appellate Tribunal held that investor rights for protection including limited veto rights, do not, per se, amount to control.

There are practical problems in transactions involving indirect acquisition and schemes of arrangement approved by the courts, in which control is consolidated without a corresponding exit opportunity for minority shareholders. In this regard, the Supreme Court decision in ***Nirma Industries Ltd. vs. SEBI*** exemplifies the continuing relevance of interpreting the takeover code.

Case Study: Indirect Acquisition and Minority Shareholder Impact in Practice

This acquisition by the Adani Group of NDTV in 2022 illustrates how the concept of legitimate economic interest (substantive fairness) has been impacted by the execution of a takeover through an intermediary company (VCPL) that was permitted to buy RRPR Holding Private

Limited's shares as a result of non-performance under the original loan contract and therefore without the direct consent of NDTV or its shareholders.

Additionally, this case illustrates how indirect or hidden takeovers through lending organizations may affect an entity's ability to comply with the provisions of India's Securities and Exchange Board of India (SEBI) Takeover Code. In 2022, the rights under the loan agreement which the Adani Group had acquired following the acquisition of VCPL were exercised that resulted in the indirect acquisition of control over the target. The resulting transaction triggered the mandatory offer requirement under regulation 3(1) of the SEBI Takeover Regulations and the Adani Group made the mandatory offer to public shareholders at the price formula.

From a regulatory perspective, the takeover complied with the formal requirements of the Takeover Code. The indirect takeover has been announced, the open offer has been made, and the price announced for the offer has also complied with SEBI rules. However, this takeover has prompted questions regarding the announcement of the open offer, the founders of NDTV sold their stakes in the company to the acquirer at a price higher than the price announced for public shareholders. Although there was no violation in this regard, questions were raised regarding the equal treatment of minority shareholders.

This case illustrates the growing concern in public takeover transactions, particularly in indirect acquisitions. While the Takeover Code ensures procedural propriety in acquisitions that includes the mandatory open offers, it does not specifically address the imbalances which are inherent in privately negotiated acquisitions for controlling shareholders. In the NDTV transaction, there were no implications of illegality.

In a broader sense, the NDTV transactions indicate that open offer obligations must be evaluated not only from a formalistic statutory angle but also from the perspective of an act which balances between commercial autonomy and investor protection. This explains why there is an increased emphasis on the substance of transactions of control and their net effect on minority investors.

Assessing the Effectiveness of the Current Open Offer Regime

The formalized process of Open Offer under the SEBI Takeover Code has clearly formalized changes involving control of listed entities and has provided certainty to parties making takeover bids or changes involving control of listed entities, thereby also providing an opportunity to minorities to exit when changes involving control are involved. This has also brought stability to the Indian mergers and acquisitions landscape.

Nevertheless, recent transactions indicate that mere procedural compliance with the obligations under the open offer regime does not always translate into substantive fairness for minority shareholders. This is particularly evident in transactions involving indirect acquisitions and a scheme of arrangement between parties in a privatisation deal and the promoters. This has highlighted limitations in schemes whereby the exit price accorded to public shareholders does not necessarily equate to the level of the control premium paid in the transaction. While such outcomes may fall within the existing legal framework, they raise questions regarding the realisation of the protective objective of the open offer procedure.

At the same time, it is necessary for the regulatory framework to maintain an appropriate degree of balance, since excessive rigidity in the form of price controls or direct intervention may serve as a disincentive for legitimate acquisitions and, as such, negatively impact the efficiency of the marketplace. This is a concern the Takeover Regulations Advisory Committee Report had flagged early on, cautioning that overly rigid pricing norms could end up discouraging genuine acquisitions rather than protecting shareholders. Judicial guidance, meanwhile, has continued to incline towards investor protection, and the steady rise in disclosure requirements and regulatory oversight has allowed the framework to grow incrementally, without compromising the flexibility needed in these transactions.

Conclusion

The Open Offer Procedure under SEBI Takeover Code remains an integral regulatory framework for M&A activities which involves listed companies in India today. Further, it seeks to balance flexibility for buyers along with protection for the minority shareholders. Among the requirements which are inherent in full disclosure in the Code, the feature provides a framework for an exit strategy for minority shareholders in control buyouts to promote increased transparency in publicly held companies being taken over.

Evolving forms of deal structure and indirect acquisition have also posed problems for deal practitioners with respect to the confirmation to established procedures. Nonetheless, under interpretation and adjudication by Parliament and subsequently by courts of law, it may be arrived at that substance rather than form continues to gain traction. Such an assessed framework would thereby ensure that due efficiency in commercial dealings continues to evolve while not chipping away at substance.