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SEBI TAKEOVER CODE: AMBIGUITIES, EXPLOITATIONS AND REFORMS

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Abstract

The SEBI Takeover Code 2011 governs substantial acquisitions and takeovers in India, aiming to ensure transparency, fairness, and minority shareholder protection. However, ambiguities in its provisions—particularly the definition of "control"—have led to regulatory loopholes and exploitation in high-profile M&A deals. This article examines key ambiguities in the Code, such as the subjective interpretation of control (including veto rights and indirect acquisitions), the creeping acquisition limit, and the challenges in enforcing provisions related to Persons Acting in Concert (PACs). Through case studies like Subhkam Ventures, Future-Reliance, Cairn-Vedanta, and NDTV-Adani, the article highlights how acquirers bypass open offer obligations by structuring transactions through indirect holdings, asset transfers, or layered ownership. The analysis also explores SEBI's regulatory evolution, explaining how the 2020 amendments addressed some gaps still some critical issues remain, such as weak minority shareholder safeguards and the lack of clarity on new-age company takeovers. The article concludes with recommendations for reform, including stricter definitions of control, enhanced PAC oversight, and robust mechanisms for indirect acquisitions to align the Code with its legislative intent of market integrity and investor protection

THE HISTORY OF THE TAKEOVER CODE

The Takeover Code's journey began with the SEBI Act, 1992, which empowered SEBI to regulate substantial share acquisitions and takeovers. In 1994, SEBI introduced the first takeover regulations, which were later reviewed by the Justice P.N. Bhagwati Committee in 1995. Based on its 1997 report, SEBI replaced the 1994 regulations with the Substantial Acquisition of Shares and Takeovers (SAST) Regulations, 1997 ("1997 Code"). The 1997 Code underwent periodic amendments to align with market developments, judicial rulings, and global practices. In 2001, a reconstituted Bhagwati Committee reviewed the Code again, leading to further amendments in 2002.

By 2009, with growing M&A activity and a decade of regulatory experience, SEBI formed the Takeover Regulations Advisory Committee (TRAC) under Mr. C. Achuthan to overhaul the framework. TRAC's recommendations, incorporating international best practices and judicial precedents, culminated in the 2011 Takeover Code, which replaced the 1997 Code. The new Code aimed to balance the interests of acquirers, shareholders, and target companies while ensuring market fairness.

THE PURPOSE OF TAKEOVER REGULATION

The purpose is to provide transparency arising out of substantial acquisition of shares and

Takeovers and to bring fairness in such transactions so as to protect the interest of the investors in securities. The Code also protects the interests of small shareholders so that in any substantial acquisition of shares, they get a fair price for the shares transferred by them.

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In the case of *K.K. Modi v. SAT*[171], the Court categorically stated that the code has been framed with a view to protect the interests of investors in securities and to promote development of and to regulate the securities market and for matters connected therewith or incidental thereto.

The code has a limited role and is not meant to ensure proper management of the business of companies or to provide remedies in the event of mismanagement. Securities Appellate Tribunal has observed that the main objective of the code is to ensure quality of treatment of opportunity to all shareholders and afford protection to them.

The Code is designed principally to ensure that shareholders in an offeree company are treated fairly and are not denied an opportunity to decide on the merits of a takeover and that shareholders in the offeree company of the same class are afforded equivalent treatment by an offeror. The Code also provides an orderly framework within which takeovers are conducted. In addition, it is designed to promote, in conjunction with other regulatory regimes, the integrity of the financial markets.

In line with international jurisprudence, Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (hereinafter referred to as the "**Takeover Code**"), the extant Indian takeover regulations also regulate the acquisition of stake in Indian listed companies and ensure transparency in the affairs of the company. Further, the

interests of the public shareholders are protected by the Takeover Code by obligating the acquirers to mandatorily provide an exit opportunity to the public shareholders in case of a takeover or substantial acquisition. Also, the Takeover Code seeks to ensure that the securities market in India operates in a fair, equitable and transparent manner.

What exactly constitutes CONTROL?

The term control has been defined in Regulation 2(1) (c)[172] of the takeover code to include the right to:

Appoint majority of the directors or to Control the management or policy decisions Exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding Or Management rights Or Shareholders agreements or voting agreements or in any other manner."

This definition is an inclusive one and not exhaustive and it has two distinct and separate features:

i) The right to appoint majority of directors or,

ii) The ability to control the management or policy decisions by various means referred to in the definition.

The scope of this definition was further discussed by SAT in the case of

Subhkam ventures pvt ltd Vs. SEBI [173]

Control according to the definition, is proactive and not reactive. It is a power by which an acquirer can command the target company to do what he wants it to do. Control really means creating or controlling a situation by taking the initiative.

The test really is whether the acquirer is in the driving seat. To extend the metaphor further, the question would be whether he controls the steering, accelerator, the gears and the brakes.

The protective provisions contained in the agreement which carries veto power the question was whether such powers can be called as exercising control

The SAT held that the purpose of such provisions is not to exercise control but to ensure that the investment made by the

[171] *K.K. Modi v.SAT* https://www.google.com/url?sa=t&source=web&rct=j&opi=89978449&url=https://www.sebi.gov.in/satorders/Modi.html%3FQUERY

[172] Regulation 2(1) (c) SEBI (substantial acquisition of shares and takeovers) Regulation 2011

[173] Subhkam ventures pvt ltd Vs. SEBI https://www.google.com/url?sa=t&source=web&rct=j&opi=89978449&url=https://www.sebi.gov.in/satorders/subhkamventures.pdf

acquirer is used as per the terms of the contract and target company does not go through any paradigm shift. Hence veto power does not constitute control

SEBI appealed against this order and when this matter was subjudice before the Supreme Court interestingly TRAC had recommended including the "ability to appoint majority of the directors or to control the management or policy decisions of the target company" along with the right to do so in the definition of "control". It emphasized including de facto control and not just de jure control.

SEBI elected to retain the definition as it is and the Supreme Court disposed the appeal filed by SEBI on the basis of mutual agreement arrived at by the parties with a specific clarification that the SAT order will not be treated as a precedent on the definition of "control".

Another important case where the meaning of "control" was discussed in detail was **The Future-Reliance Deal (2021-23): A Test of "Control"--**

The ₹24,713 crore Future-Reliance deal highlighted ambiguities in the Takeover Code's definition of "control." Future Group agreed to sell its retail assets to Reliance Retail in 2020. Amazon, holding a 49% stake in Future Coupons (a Future Group entity), contested the deal, arguing it violated its right of first refusal (RoFR) and contractual terms. Future claimed SEBI's open offer rules didn't apply since Reliance acquired assets, not shares, directly. Amazon countered that the transaction effectively transferred "control" of Future Retail (a listed entity) to Reliance, triggering the Takeover Code.

While SEBI and the Supreme Court intervened, Future's bankruptcy ultimately derailed the deal. The case exposed a critical gap: the Code lacks clear provisions for asset transfers that indirectly shift control of listed companies, leaving room for strategic circumvention of open offer obligations.

The SEBI (Substantial Acquisition and Takeover regulations) 2011 States some mandatory triggering points Whenever an acquirer individually or along with PAC (person acting in concert) acquirers the prescribed limit of:

1. Shares

2.Voting rights

3.Control in the target company it has to mandatorily give an open offer to the public shareholders.

Now that we are familiar that acquisition can be done by three modes. Let us discuss each one of these in detail.

DIRECT ACQUISITION OF SHARES/VOTING RIGHTS/CONTROL

Initial trigger threshold (regulation 3)[174]

Regulation 3(1) casts an obligation on the acquirer to make a public announcement of an open offer for acquiring shares of any target company where acquirer acquires shores or voting rights in a target company which taken together with shares or voting rights, if any, held by him and by PACs with him in such target-company, entitle them to exercise 25% or more of the voting rights in such target company, However, regardless of the level of shareholding and acquisition of shares, acquisition of control-over a target company would require the acquirer to make an open offer.

The open offer obligation would also apply to acquisition of shares by any person from other persons acting in concert with him such that the individual shareholding of the person acquiring shares equals or exceeds the stipulated threshold of 25% although the aggregate shareholding along with persons acting in concert may remain unchanged[175].

Creeping Acquisition Trigger

Creeping acquisition means slow and steady acquisition of shores by the acquirer in the

[174] Regulation 3(1) of the SEBI (substantial acquisition of shares and takeovers) Regulation 2011
[175] Regulation 3(2) of the SEBI (substantial acquisition of shares and takeovers) Regulation 2011

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target company. In creeping acquisition acquirer can acquire max 5% voting rights of Target Company in each financial year.

An acquirer who (together with PACs) holds 25% or more voting rights in a target company but less than the maximum permissible non-public shareholding [i.e., Maximum Permissible Non-Public (Promoters') Shareholding is 75% and Minimum Permissible Public shareholding is 25%], is allowed to acquire additional voting rights in the target company to the extent of upto 5% within a financial year ending on 31st March, without making an open offer [Regulation 3(2)]. If he acquires more than 5% additional voting rights in a financial year ending on 31st March, he will have to make an open offer. This is subject to their (acquirer and PACS) aggregate post acquisition shareholding not exceeding the maximum perm non-public shareholding.

Thus, creeping acquisition can be made at the maximum rate of 5% in any one financial without complying with the requirement of mandatory public offer by way of announcement, provided that the post-acquisition shareholding of acquirer together persons acting in concert with him shall not increase beyond 75%

The open offer obligation would also apply to acquisition of shares by any person from other persons acting in concert with him such that the individual shareholding of the person acquiring shares equals or exceeds the stipulated threshold of 5% although the aggregate shareholding along with persons acting in concert may remain unchanged.

INDIRECT ACQUISTION: A Regulatory Gap and Its Resolution

The original 1994 Takeover Code did not account for indirect acquisitions - situations where control of a listed company is gained through acquiring its unlisted holding company or parent entity. This critical oversight became apparent as SEBI gained regulatory experience. The Bhagwati Committee, in its review, identified this loophole and recommended expressly recognizing indirect acquisitions as a distinct concept. The committee advocated for balanced regulation - avoiding excessive restrictions that might stifle legitimate M&A activity, while preventing covert takeovers that circumvent shareholder protections.

This recommendation led to the incorporation of indirect acquisition provisions in subsequent regulations, closing a significant gap in India's takeover framework. The reform ensured that control changes, whether direct or indirect, would trigger appropriate disclosure and offer requirements to safeguard minority shareholders.

The committee's recommendations led to the recognition of indirect Acquisitions as a distinct concept under the Takeover Code 1997. Originally, the regulations stipulated that 'indirect acquisitions' involved the acquisition of shares or control in a listed company by way of acquisition of control in its holding company[176]. The provision was eventually amended in 2002 to Broaden the scope of the term – it would now include indirect acquisitions through all companies, whether these be holding companies, or otherwise[177]. Separately, the Takeover Code 1997 made the acquisition of 'control' over a listed company a trigger for a mandatory takeover bid, which could occur directly or indirectly[178].

The introduction of the notion of indirect acquisitions gave rise to the question of when an indirect acquisition would occur, leading to a mandatory takeover bid obligation falling upon an acquirer.

Consider the following

Example - company A holds a 35% stake in a listed company, B (the target).

[176] Takeover Code 1997, explanation to regs 10 and 11 ("…acquisition shall mean and include:
(b) indirect acquisition by virtue of acquisition of holding companies, whether listed or
unlisted, whether in India or abroad.").
[177] Takeover Code 1997, reg 12
[178] Takeover Code 1997, reg 2(1) (c).

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Company C acquires a 60% stake and a controlling interest in company A.

In such a situation, would company C be required to make a mandatory takeover bid for the shares in company B? Competing arguments were made for the adoption of one of the following two tests for making this determination:

a) Proportionate interest test: This test involves a mathematical calculation of the acquirer's proportionate interest in the target company[179].

In the example above, therefore, company C's proportionate interest in company B would be understood as 60% of 35%, i.e., 21% - this would, therefore, not give rise to a mandatory takeover obligation.

b) Effectuality test: This test involves a determination of whether the upstream acquisition of shares, voting rights, or control in the intermediate company would have an effect on the manner in which the intermediate company would exercise its voting rights or control in

the target company. Going back to our example, since company C, by virtue of its acquisition of the 60% stake and controlling interest in company A, would also be in a position to influence the manner in which company A exercises its control and voting rights in B. Effectively, company C does not merely control 21% of company B's voting rights, as would be its proportionate share, but the full 35% that company A holds. This would result in a mandatory takeover obligation being imposed on company C.

The proportionate interest test had gained acceptance initially and was predominantly relied upon by those within the industry. However, others believed that this test lacked the subjectivity required to make a determination on the indirect acquisition of control since it was merely reflective of the economic benefit to the acquirer and failed to take into account the voting and control that could be exercised by them. This led to the development of the more robust effectuality test. This test gained significant credence once it was adopted by SEBI in the NRB Bearings order under the provisions of the Takeover Code 1997.

In NRB Bearings[180], SEBI's ruling in the NRB Bearings case established a critical precedent for indirect acquisitions. Here's how the case unfolded:

US-based Timken Company (TC) entered into an agreement to acquire voting securities in Nadella SA, a French subsidiary of Bermuda-incorporated Ingersoll-Rand (IR). The key factor was that Nadella held a significant 26% stake in NRB Bearings, an Indian listed company.

When this transaction came before SEBI, the regulator had to determine whether TC's indirect acquisition through Nadella triggered mandatory open offer requirements. SEBI took a firm position - by gaining control over Nadella, TC effectively acquired control over Nadella's entire 26% voting rights in NRB Bearings, not just a proportional share. This decision was ground-breaking because it established that:

1. Control over an intermediary entity means control over all its holdings in the target company
2. The "effectuality test" - focusing on actual control rather than proportional ownership - became the standard
3. Acquirers could no longer structure deals through intermediaries to avoid takeover obligations

The NRB Bearings case thus became a landmark judgment that shaped India's takeover regulations by closing a major loophole in indirect acquisitions. SEBI's ruling ensured that the spirit of takeover regulations -

[179] Nishith Desai Associates, 'Public M&As in India: Takeover Code Dissected' (*Nishith Desai Associates,* August 2013) <http://www.nishithdesai.com/fileadmin/user_upload/pdfs/Ma%20Lab/Takeover%20Code%20Dissected.pdf> accessed 1 April 2020

[180] NRB Bearings *Timken Co., In re (Acquisition of Shares/Voting Rights/Control of* NRB Bearings India *Ltd. and SNL Bearings Ltd.)*, 2003 SCC Online SEBI 84

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protecting minority shareholders - couldn't be circumvented through layered corporate structures.

The effectuality test became a norm and standard after the NRB case before this the position regarding such acquisition was quite unclear

For example, let's take a look at the Cairns-Vedanta deal which took place in 2011:

Background: Vedanta acquired Cairn UK, which held 60% in Cairn India (listed in India).

Vedanta argued that since it was buying Cairn UK (not directly Cairn India shares), no open offer was needed. SEBI initially exempted Vedanta from an open offer, but later reversed its decision after investor backlash.

Vedanta had to make a minority shareholder offer under pressure. The code did not clearly regulate upstream mergers affecting Indian listed firms.

DEEMED DIRECT ACQUISITION

Under Regulation 5(2)[181] of SEBI's Takeover Code, an indirect acquisition is treated as a direct acquisition if:

a. the proportionate net asset value of the target company as a percentage of the consolidated net asset value of the entity or business being acquired;

b. the proportionate sales turnover of the target company as a percentage of the consolidated sales turnover of the entity or business being acquired; or

c. the proportionate market capitalisation of the target company as a percentage of the enterprise value for the entity or business being acquired;

is in excess of eighty per cent, on the basis of the most recent audited annual financial statements, such indirect acquisition shall be regarded as a direct acquisition of the target company for all purposes of these regulations including, without limitation, the obligations relating to timing, pricing and other compliance requirements for the open offer. This rule prevents acquirers from bypassing open offer obligations by structuring transactions through holding companies or intermediaries.

In the NDTV case[182], the Adani Group's acquisition of a 29.18% stake through Vishvapradhan Commercial Private Limited (VCPL) triggered an open offer for an additional 26% stake, as per regulations. This indirect acquisition was deemed a direct acquisition because it triggered the mandatory open offer requirements under SAST.

More detailed breakdown of the case:-

VCPL's Role: Vishvapradhan Commercial Private Limited (VCPL), a little-known company, had provided an interest-free loan of ₹403 crore to NDTV's promoter entity, RRPR Holdings, in 2009. In exchange, RRPR issued convertible warrants allowing VCPL to acquire a 99.99% stake in RRPR (which held 29.18% in NDTV) if the loan remained unpaid.

Adani's Move: In August 2022, Adani acquired VCPL and exercised the warrants, gaining indirect control over NDTV's 29.18% stake

The NDTV takeover by Adani Group qualifies as a deemed direct acquisition under SEBI's Takeover Regulations due to the disproportionate significance of NDTV relative to the intermediary entity (VCPL) and the control mechanism used. Here's the breakdown:

How NDTV's Acquisition Fits the Criteria of deemed direct acquisition

A. Financial Dominance of NDTV Over VCPL

- VCPL was a shell company with minimal operations, while NDTV was a major media conglomerate with significant assets and revenue.

[181] Regulation 5(2) of the SEBI (substantial acquisition of shares and takeovers) Regulation 2011

[182] NDTV case https://www.google.com/url?sa=t&source=web&rct=j&opi=89978449&url=https://www.sebi.gov.in/sebi_data/commondocs/aug-2022/NDTV_DPS_p.pdf

- NDTV's financial metrics (NAV, turnover, etc.)Exceeded 80% of VCPL's consolidated value, triggering the "deemed direct" rule.

B. Control Mechanism

- Adani acquired VCPL, which held convertible warrants for RRPR Holdings (NDTV's promoter entity).
- By exercising these warrants, Adani gained 29.18% indirect stake in NDTV, effectively controlling it despite not directly buying NDTV shares 612.
- SEBI's "chain principle" (from *Technip v. SMS Holdings*) applies: Control over VCPL = Indirect control over NDTV 2.

Regulatory Consequences

Since the acquisition was deemed direct:

1. Mandatory Open Offer: Adani had to make an open offer for 26% of NDTV shares (even though the acquisition was indirect) 1213.
2. Pricing Rules: The offer price was calculated under Regulation 8, factoring in NDTV's market value, not VCPL's

Key Precedents Supporting This Classification

- Linde AG/Praxair: SEBI rejected exemptions for upstream mergers affecting downstream Indian subsidiaries, reinforcing strict "deemed direct" interpretations.
- NRB Bearings Case: Confirmed that proportionality (e.g., minority stakes in intermediaries) doesn't exempt acquirers from open offers if control is effectively transferred.

SEBI's jurisprudence treats such **layered takeovers** as direct if they undermine shareholder protections

Key takeaways and suggestions for stricter achievement of legislative intention of the Code:

"Control" is still a grey area – Companies exploit veto rights, indirect acquisitions, and asset sales to bypass open offers.

PACs & creeping acquisition limits are weakly enforced – Hostile takeovers can happen through rapid market purchases.

2020 Amendments has tightened some rules (e.g., clearer PAC definitions)

But asset transfers, indirect control, and creeping acquisitions still need stricter regulation.

Indirect acquisitions remain a loophole – Buying foreign parents to control Indian firms is a regulatory blind spot and hence regulation covering such blind spots should be taken into consideration.

Conclusion

The SEBI Takeover Code, while a cornerstone of India's financial regulation, remains a work in progress. Its effectiveness hinges on closing interpretative gaps—whether in defining "control," regulating indirect acquisitions, or preventing stealthy creeping takeovers. The judiciary and SEBI have made strides, but market ingenuity often outpaces regulation, as seen in deals like Vedanta-Cairn and Adani-NDTV. True reform demands not just reactive amendments but anticipatory governance—clearer thresholds, stricter PAC oversight, and explicit rules for asset transfers. Only then can the Code fulfill its promise: a market where takeovers are fair, transparent, and free from exploitation. The path forward lies in precision, enforcement, and unwavering commitment to minority shareholders.