

BEFORE THE SECURITIES APPELLATE TRIBUNAL
MUMBAI

Appeal No. 111 of 2008

Date of decision : 22.07.2009

1. Eight Capital Master Fund Ltd.
2. Spinnakar Global Opportunity Fund Ltd.
3. Spinnakar Global Emerging Markets Fund Ltd.
4. Spinnakar Global Strategic Fund Ltd. ... Appellants

Versus

Securities and Exchange Board of India Respondent

Mr. P. N. Modi, Advocate for Appellants.

Mr. J. J. Bhatt, Senior Advocate with Ms. Harshada Nagare,
Advocate for the Respondent.

Coram : Justice N.K. Sodhi, Presiding Officer
Samar Ray, Member

Per : Justice N.K. Sodhi, Presiding Officer

Pennar Industries Limited is the target company. It is registered and incorporated under the Companies Act, 1956 with its registered office in Hyderabad. Its shares are listed on the Bombay Stock Exchange Limited (BSE). On March 3, 2006 the board of directors of the target company (hereinafter referred to as BoD) passed a resolution to convene an extraordinary general meeting (EGM) for seeking the approval of its shareholders for allotting convertible debentures to the appellants on preferential basis in order to raise additional resources amounting to Rs.122.40 crores to be utilized for returning the target company's debt and also for additional working capital requirements. A notice dated March 3, 2006 was issued under section 81(1A) of the Companies Act to the shareholders, inter alia, informing them that an EGM would be held on March 27, 2006 for seeking their approval for allotment to the appellants on preferential basis 50,32,700 Part A convertible debentures of Rs.100 each carrying interest of 7 per cent per annum which will be compulsorily and automatically

converted within 18 months from the date of allotment into 3,41,20,000 equity shares of Rs.5 each at a premium of Rs.9.75 per share. Further, as regards Part B optionally convertible debentures, the appellants had the option to convert them into equity shares of Rs.5 each at a conversion price of Rs.50 per share. We are not concerned with these Part B optionally convertible debentures in the present appeal. The EGM was held as scheduled on March 27, 2006 and the resolutions were passed. For the issue of convertible debentures and optionally convertible debentures, the target company also made an application to BSE seeking its in-principle approval for the same in terms of its listing agreement. On June 26, 2006 BSE gave its in-principle approval.

2. In pursuance to the approval granted by the shareholders for the allotment of Part A convertible debentures, the Debenture Committee of the BoD allotted to the appellants debentures in its meeting held on July 21, 2006. On the same day, a debenture subscription agreement was executed between the target company and the appellants. As already noticed above, the debentures could be converted into equity shares at any time within 18 months from the date of their allotment but they had necessarily to be converted on the expiry of 18 months.

3. Appellants no. 3 and 4 partly exercised their conversion option on December 24, 2007 with respect to 19,05,641 and 4,24,210 Part A convertible debentures respectively. Accordingly 1,29,19,600 and 28,76,000 equity shares were allotted to Appellants no. 3 and 4 respectively. This allotment represented 14.6 per cent (less than 15 per cent) of the expanded paid up equity share capital of the target company. On January 26, 2008 when the 18 months period expired, the remaining debentures with the appellants were automatically converted into equity shares raising their total shareholding in the target company from 14.6 per cent to 26 per cent. It is common ground between the parties that all the four appellants while acquiring the debentures/shares of the target company were acting in concert with each other. Regulation 10 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (for short the takeover code) provides that no acquirer shall acquire shares which, taken together with shares already held by him or

by persons acting in concert with him, entitles such acquirer to exercise 15 per cent or more of the voting rights in a company unless such acquirer makes a public announcement to acquire shares of such company in accordance with the takeover code. Regulation 14 of the takeover code prescribes the timing of the public announcement of offer. In the case of an acquirer acquiring securities, the public announcement in terms of Regulation 10 has to be made not later than 4 working days before he acquires the voting rights on such securities upon conversion or exercise of option as the case may be. Since post conversion of the Part A convertible debentures on January 26, 2008 raised the shareholding of the appellants to 26 per cent, Regulation 10 of the takeover code got triggered and the appellants were required to make a public announcement to acquire further shares of the target company. They made a public announcement through YES Bank Ltd. as their merchant banker on January 22, 2008 (4 days before the conversion on January 26, 2008) to acquire shares from the public shareholders upto 2,52,95,496 fully paid up equity shares of the face value of Rs.5 each representing 20 per cent of the voting paid up equity share capital of the target company at a price of Rs.14.75 per fully paid up equity share payable in cash. In the public announcement, the price at which the shares were offered to the shareholders was calculated at Rs.14.75 per share. After the public announcement was made and within the time prescribed by Regulation 18 of the takeover code, the appellants through their merchant banker prepared a draft of the letter of offer and the same was sent to the Securities and Exchange Board of India (for short the Board) for its comments. The proviso to Regulation 18(2) provides that if the Board on receipt of the letter of offer specifies changes, if any, in the letter of offer, merchant banker and the acquirer shall carry out such changes before the letter of offer is dispatched to the shareholders. The Board examined the letter of offer and gave its comments as per letter dated August 29, 2008 regarding the offer price. The observations of the Board are as under:

- “5. Offer Price/Financial Arrangement
 - a. **re-calculate the offer price by reckoning the date of PA as the reference date in terms of regulation 20 and to offer the revised price as re-calculated to all the shareholders.**
 - b. to make the changes with regard to the offer price at all applicable places in the offer document.....”
(emphasis supplied)

The appellants were advised to make a corrigendum to the public announcement in all the newspapers in which it originally appeared after incorporating the comments. Feeling aggrieved by these comments by which the Board directed the appellants to recalculate the offer price, they have filed the present appeal.

4. The dispute between the parties is essentially with regard to the method of determining the offer price at which the appellants are required to purchase the shares from the existing shareholders of the target company. Before we deal with the rival contentions of the parties, it is necessary to refer to the relevant provisions of the takeover code which govern the issue. The term “shares” has been defined in clause (k) of Regulation 2(1) of the takeover code which reads as under:

“(k) “shares” means shares in the share capital of a company carrying voting rights and includes any security which would entitle the holder to receive shares with voting rights but shall not include preference shares.”

Relevant parts of Regulations 10, 14, 18, 20(4) & (11) which are material for the issue in question are also reproduced hereunder for facility of reference:-

“Acquisition of fifteen per cent or more of the shares or voting rights of any company;

10. No acquirer shall acquire shares or voting rights which (taken together with shares or voting rights, if any, held by him or by persons acting in concert with him), entitle such acquirer to exercise fifteen per cent or more of the voting rights in a company, unless such acquirer makes a public announcement to acquire shares of such company in accordance with the regulations.

Timing of the public announcement of offer.

14. (1) The public announcement referred to in regulation 10 or regulation 11 shall be made by the merchant banker not later than four working days of entering into an agreement for acquisition of shares or voting rights or deciding to acquire shares or voting rights exceeding the respective percentage specified therein:

(2) In the case of an acquirer acquiring securities, including Global Depository receipts or American Depository Receipts which, when taken together with the voting rights, if any already held by him or persons acting in concert with him, would entitle him to voting rights, exceeding the percentage specified in regulation 10 or regulation 11, the public announcement referred to in sub-regulation (1) shall be made not later than four working days before he acquires voting rights on such securities upon conversion, or exercise of option, as the case may be.

Submission of letter of offer to the Board.

18. (1) Within fourteen days from the date of public announcement made under regulation 10, 11 or 12 as the case may be, the acquirer shall, through its merchant banker, file with the Board, the draft of the letter of offer containing disclosures as specified by the Board.

(2) The letter of offer shall be dispatched to the shareholders not earlier than 21 days from its submission to the Board under sub-regulation (1):

Provided that

Offer price.

20.(1) The offer to acquire shares under regulation 10, 11 or 12 shall be made at a price not lower than the price determined as per sub-regulations (4) and (5).

(2).....

(3).....

(4) For the purposes of sub-regulation (1), the offer price shall be the highest of-

(a) the negotiated price under the agreement referred to in sub-regulation (1) of regulation 14;

(b) price paid by the acquirer or persons acting in concert with him for acquisition, if any, including by way of allotment in a public or rights or preferential issue during the twenty-six week period prior to the date of public announcement, whichever is higher;

(c) the average of the weekly high and low of the closing prices of the shares of the target company as quoted on the stock exchange where the shares of the company are most frequently traded during the twenty-six weeks or the average of the daily high and low of the prices of the shares as quoted on the stock exchange where the shares of the company are most frequently traded during the two weeks preceding the date of public announcement, whichever is higher:

Provided that

(11) The letter of offer shall contain justification or the basis on which the price has been determined.

Explanation:

(i)

(ii) Where the public announcement of offer is pursuant to acquisition by way of firm allotment in a public issue or preferential allotment, the average price under clause (c) of sub-regulation (4) shall be calculated with reference to twenty-six week period preceding the date of the board resolution which authorised the firm allotment or preferential allotment.

(iii)

(iv)”

5. The primary grievance of the appellants is that the Board was not justified in directing them to recalculate the offer price by reckoning the date of public announcement as the reference date in terms of Regulation 20 of the takeover code. Their contention is that they calculated the offer price of Rs.14.75 per share having regard to the date on which the BoD passed the resolution to convene the EGM under section 81(1A) of the Companies Act for seeking approval of the shareholders for allotment of Part A convertible debentures to the appellants on preferential basis. This meeting of the BoD was held on March 3, 2006 and, according to the appellants, it was this board meeting “**which authorised the preferential allotment**” to them and that the offer price was rightly calculated with reference to this date. In the alternative, Shri P. N. Modi learned counsel for the appellants argued that the date for determining the offer price could be the date of the board meeting in which the BoD made the allotment of Part A convertible debentures to the appellants. This meeting was held on July 21, 2006 and, according to Shri Modi, it was on this day when the preferential allotment of convertible debentures was made to the appellants and, therefore, this could be the date with reference to which the offer price may be calculated. He referred to the definition of shares in clause (k) of Regulation 2(1) of the takeover code and contended that the compulsorily convertible debentures which entitled the appellants to receive shares with voting rights were ‘shares’ within the meaning of the takeover code. On the other hand, Shri J. J. Bhatt learned senior counsel appearing for the Board argued that the Board was right in directing the appellants to recalculate the offer price by reckoning the date of public announcement as the reference date in terms of Regulation 20 of the takeover code. The public announcement was made on January 22, 2008 and, according to the learned senior counsel, it is with reference to this date that the offer price has to be calculated. In the alternative, Shri Bhatt strenuously contended that the date with reference to which the offer price could be determined has to be the date of the board resolution authorizing preferential allotment to the appellants and this, according to him, was done by the BoD in their meeting held on January 26, 2008. Referring to Regulation 10 of the takeover code, the learned senior counsel pointed out that this code gets triggered only when the acquirer acquires 15 per cent or more of the

voting rights in a company and not on the acquisition of shares which do not carry voting rights. The argument is that the appellants acquired the voting rights only on January 26, 2008 when the debentures held by them were converted into equity shares which carried voting rights, and according to Shri Bhatt, it is this date with reference to which the offer price has to be calculated.

6. From the rival contentions of the parties, the question that requires consideration is as to what should be the reference date for the determination of the offer price which the appellants as acquirers are required to offer to the existing shareholders of the target company. Regulation 20 of the takeover code deals with the offer price. Clause (1) thereof makes it clear that the offer to acquire shares under Regulation 10 shall be made at a price not lower than the price determined as per sub-regulations (4) and (5). Sub-regulation (4) is the one with which we are concerned in the instant case. It has three clauses (a), (b) and (c) and they prescribe three different modes of calculating the offer price and the highest of the three prices shall be the offer price. We are really concerned with the method prescribed in clause (c). It lays down that the average of the weekly high and low of the closing price of the shares of the target company during twenty-six weeks or the average of the daily high and low of the prices during two weeks preceding the date of public announcement is to be worked out and the highest of the two shall be the offer price. It is thus clear that this clause pitches the offer price with reference to the date of public announcement made by the acquirer. Sub-regulation (11) of Regulation 20 requires the letter of offer to contain justification or the basis at which the price has been worked out. Explanation (ii) to this sub-regulation is relevant to the price determination under sub-regulation (4) of Regulation 20 and is an exception thereto. It provides that where the public announcement is made pursuant to acquisition by way of firm allotment in a public issue or preferential allotment, then the offer price under sub-regulation 4(c) is to be worked out with reference to twenty-six week period preceding the date of **‘the board resolution which authorised the firm allotment or preferential allotment.’** In the case before us, the compulsorily convertible debentures were allotted to the appellants on a preferential basis after the shareholders of the target company had authorised the BoD in the EGM held on March 27, 2006. The offer price

has, therefore, to be determined with reference to twenty-six week period preceding the date of the board resolution which authorized the preferential allotment.

7. The next question that arises is when did the BoD authorise the preferential allotment in favour of the appellants. Before we answer this question, we may dispose of an ancillary issue that arose during the course of the hearing. Explanation (ii) to Regulation 20(11) refers to “preferential allotment”. Does allotment mean allotment of securities carrying voting rights or even those which do not carry voting rights. The answer is quite clear. When we read the Explanation with the other clauses of Regulation 20 and keep in mind the fact that the takeover code gets triggered only on the acquisition of voting rights and not otherwise, the allotment referred to in the Explanation would obviously mean allotment of securities carrying voting rights. We have, therefore, to determine the date of BoD meeting in which they authorised the allotment of shares carrying voting rights. As already noticed, the appellants contend that this happened on March 3, 2006 when the BoD resolved to convene the EGM for March 27, 2006 for the allotment of convertible debentures. According to the appellants the preferential allotment was, in any case made to them by the BoD on July 21, 2006 and at the most this could be the date when they authorised the preferential allotment. The learned senior counsel appearing for the Board seriously disputes this position and contended that the date of public announcement could well be taken as the date on which the preferential allotment could be said to have been authorised by the board of directors. He strenuously contended that, in any case, January 26, 2008 would be the date on which the preferential allotment was authorised by the board of directors as it was on that date that the allotment of shares were made to them on the conversion of the warrants.

8. We have given our thoughtful consideration to the rival contentions of the parties and find merit in the alternative contention of Shri J.J. Bhatt, learned senior counsel for the Board. March 3, 2006 cannot be the date as in that meeting the BoD had only resolved to convene the EGM to enable the shareholders to consider the preferential allotment in favour of the appellants. Hence that meeting cannot be said to

be one in which the BoD authorised the preferential allotment. How could the board of directors authorise the preferential allotment when the shareholders had yet to consider the issue in the EGM which was to be held later. We have, therefore, no hesitation in rejecting the first contention of Shri Modi. Again, we find no merit in his second contention either. July 21, 2006 is the other date to which reference has been made by the learned counsel for the appellants. He contends that on this date the BoD in their meeting had allotted the compulsorily convertible debentures to the appellants after obtaining sanction from the shareholders. Referring to clause (k) of Regulation 2(1) of the takeover code, he argued that these debentures which entitled the appellants to receive shares with voting rights were shares within the meaning of the takeover code and, therefore, July 21, 2006 is the date on which the BoD authorised the preferential allotment. The argument looks attractive but we have not been able to persuade ourselves to accept the same. Undoubtedly, the compulsorily convertible debentures were allotted to the appellants by the BoD in their meeting on July 21, 2006 and even though these debentures were shares for the purposes of the takeover code, they did not carry any voting rights on that date. The BoD meeting of July 21, 2006 did not, therefore, authorise the preferential allotment of shares carrying voting rights. The voting rights which triggered the takeover code were acquired by the appellants only on January 26, 2008 when the period of 18 months expired and the compulsorily convertible debentures got converted automatically and the BoD in their meeting on that day allotted equity shares to the appellants. It is on this date the BoD authorised the preferential allotment to the appellants within the meaning of Explanation (ii) to Regulation 20(11). It is with reference to this date (January 26, 2008) that the offer price shall have to be worked out. We cannot agree with the Board that the offer price has to be worked out with reference to the date of public announcement. The date of public announcement is not relevant because allotment in the present case was made on a preferential basis and, therefore, Explanation (ii) gets attracted. As per this explanation the price has to be worked out with reference to the date on which the BoD authorised the preferential allotment. We have already held that that date is January 26, 2008. The appellants shall have to work out the offer price accordingly. The

directions of the Board in para 5(a) of the impugned communication requiring the appellants to re-calculate the offer price with reference to the date of public announcement in terms of Regulation 20 cannot be sustained as it is contrary to the plain language of Explanation (ii) to Regulation 20(11) of the takeover code. The same is accordingly set aside. The appellants are directed to re-calculate the offer price by reckoning January 26, 2008 as the date in terms of Explanation (ii) as discussed hereinabove and offer the revised price to all the shareholders.

9. Before parting, we may refer to our order in *Sohel Malik v. Securities and Exchange Board of India* Appeal no. 108 of 2008 decided on 15.10.2008 which was cited by the learned senior counsel for the Board. It is on similar facts and involves an identical question of law. The learned counsel for the appellant tried to distinguish it on facts but we do not find any material difference. In that case, the convertible warrants were converted into equity shares by the board of directors in their meeting on 28.6.2008 and we held this date to be date for computing the offer price and we did not agree with the Board that the price had to be recalculated with reference to the date of public announcement.

In the result, the appeal is disposed off as above with no order as to costs.

Sd/-
Justice N.K. Sodhi
Presiding Officer

Sd/-
Samar Ray
Member

dd/- 220709

Prepared & compared by