

M&A Hotline

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INTER SE TRANSFER BETWEEN PROMOTERS – NO EXEMPTION IN THE FIRST THREE YEARS AFTER LISTING SAYS SEBI

INTRODUCTION

The Securities and Exchange Board of India (“SEBI”) has taken a conservative stand in its interpretative letter¹ dated December 5, 2012 issued to Commercial Engineers and Body Builders Company Ltd. (“CEBBCO”). The letter clarifies that the exemption for inter se transfer of shares amongst promoters can only be availed by persons who are disclosed as promoters in the shareholding pattern of the target company for the last three years even in cases where the target company has not completed three years of listing on a stock exchange.

FACTS

Equity shares of CEBBCO were listed on NSE and BSE on October 18, 2010. The promoters and the promoter group collectively hold 55.81% of the paid-up share capital of CEBBCO. Mr. Ajay Gupta (“AG”), one of the promoters of the Company, intends to sell shares of CEBBCO constituting 17.61% of the paid up share capital to Mr. Kailash Gupta (“KG”) another promoter of the Company and also father in law of AG. Since, the proposed transfer will trigger the open offer obligations under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (the “Takeover Code”), parties want to avail the benefit of exemption under Regulation 10(1)(a)(ii) of the Takeover Code.

Per Regulation 10(1)(a)(ii) of the Takeover Code, acquisition pursuant to inter se transfer of shares amongst persons named as promoters in the shareholding pattern filed by the target company in terms of the listing agreement or Takeover Code for not less than three years prior to the proposed acquisition is exempt from mandatory open offer requirements subject to prescribed pricing and disclosure conditions.

Both AG and KG have been identified as promoters of CEBBCO in all the shareholding patterns filed with NSE and BSE since the date of listing of CEBBCO. AG has been a shareholder/promoter of CEBBCO since December 23, 2006 while KG has been a shareholder/ promoter of CEBBCO since October 3, 2005.

ISSUE

CEBBCO became a listed company only on October 18, 2010 and therefore, it is impossible for the company to have filed shareholding pattern for three years prior to the proposed acquisition. Though KG and AG had been promoters of CEBBCO for more than three years, since CEBBCO was listed for only 2 years prior thereto, AG and KG had been reflected as promoters in the filings with the stock exchanges for only two years. Accordingly CEBBCO approached the SEBI to seek guidance as to whether a transfer of shares from AG to KG would be for the exemption under Regulation 10(1)(a)(ii) of the Takeover Code.

ORDER

CEBBCO had argued that the condition of continuous disclosure of persons as promoters for three years prior to the proposed transaction has been prescribed under Regulation 10(1)(a)(ii) to ensure that only persons holding long term interests in target companies were eligible for the exemption. If such a condition was not prescribed then persons could identify themselves as promoters immediately prior to the transfer and would avail the benefit of the exemption under Regulation 10(1)(a)(ii). In this case AG and KG were promoters of CEBBCO since December 23, 2006 and October 3, 2005, respectively and they clearly held long term interest in the target company.

CEBBCO also clarified that it was impossible to mention AG and KG as promoters in its shareholding pattern for three years as the company was listed only two years prior thereto. It was argued that the AG and KG should not be denied the exemption under Regulation 10(1)(a)(ii) of the Takeover Code merely on account of a technical impossibility. CEBBCO suggested that the emphasis should be on the spirit of the provision but not on the literal interpretation of the provision.

SEBI, however, did not accept the arguments of CEBBCO and clarified that the exemption under Regulation 10(1)(a)(ii) of the Takeover Code could be availed only if all the compulsory conditions were duly fulfilled. One of the prescribed conditions is that the transferor and the transferee should have been identified as promoters of the target company in the shareholding pattern filed under the listing agreement or the Takeover Code for three years prior to the acquisition. If this condition is not fulfilled for any reason whatsoever, inter alia including if the target company was not listed for three years then the exemption under Regulation 10(1)(a)(ii) of the Takeover Code cannot be availed.

ANALYSIS

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In light of this interpretative letter, it would appear that the earliest the exemption under Regulation 10(1)(a)(iii) of the Takeover Code can be availed by promoters desirous of transferring shares inter-se is after 3 years of listing of the target company. Though SEBI has relied on literal interpretation of Regulation 10(1)(a)(ii) of the Takeover Code, such situations may be fit for seeking specific exemption from SEBI under Regulation 11 of the Takeover Code. It may also be noted that in the present set of facts since KG is AG's father in law, the proposed transaction may also be eligible for automatic exemption under Regulation 10(1)(a)(i) of the Takeover Code, being inter se transfer between two 'immediate relatives'. The definition of 'immediate relative' under Regulation 2 (1)(l) of the Takeover Code includes the father of the spouse of a person.

— Arun Scaria & Simone Reis
You can direct your queries or comments to the authors

¹ http://www.sebi.gov.in/cms/sebi_data/commondocs/commercialsebiletter_p.pdf

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