CHAPTER - IX

LISTING AGREEMENT OF STOCK EXCHANGE RELATING TO TAKEOVERS
This Chapter analyses how the interests of shareholders in Merger of Corporate Companies are affected by listing agreement and correct decisions.

Indian Stock Exchanges play an important role to safeguard the interests of shareholders of Corporate Companies. Listing agreement between Corporate Companies and Stock Exchanges is already in vogue and it is applicable to all Indian Stock Exchanges. Clause 40 of the Listing agreement stipulates that certain rules must be followed in the acquisition of shares of another company or in the "Security of Effective Control" of the management of the target company.

The basic features of clause 40 are somewhat similar to those of the London City code and the safeguards contemplated are:-

1) A public announcement must be made through newspapers (English and vernacular) in the "PREScribed MANNER". The Stock Exchanges where the shares are listed must be notified immediately.

2) After the negotiation is completed both the purchaser and seller must inform the concerned stock exchanges about the conclusion of the deal.
3) Thereafter, an offer should be made to the remaining members in the form of a circular containing details regarding the identity of the purchaser, source of funds, reasons for the purchase and future proposals etc. The Circular has to be approved by the Regional Stock Exchange where the registered office of the company is situated.

4) Such an offer must be made within two weeks from the date of approval and has to be kept open for at least six weeks from the date of the offer. The offer, if amended, will have to be kept open for a further period of six weeks.

5) If as a result of purchase of shares there is a change in the management of the company, this must be intimated to the Government.

It may be noted from the above clause that the approval has to be obtained before the requisition of shares takes place. However, in the RPG-SPENCER Deal, the Madras Stock Exchange was informed after the shares were acquired from the Bhabha family. Stock Exchanges have power to delist the shares of the company with the terms of clause 40. Delisting of shares by Stock Exchanges may often help the company who committed the default. If the Spencer's shares had been delisted, the minority shareholders of Spencer & Co.Ltd. would have been affected.
The existing regulations prohibit anyone acquiring 25% of the share capital of the target company. CHABRIAS circumvented this regulation by acquiring 24.9% of the share capital of General Electric Company of India Ltd.

The Clause 40 of the Listing Agreement is not adequate to grant protection to minority shareholders. This view is also supported by Mr. E R Krishnamurthy, Chairman, Advisory Committee on Capital Issues Control, Ministry of Finance, Government of India in his article on "CAN MINORITY Holders' BE SAFEGUARDED?" (FORTUNE INDIA 10 APRIL 89). In his article, he states that in the case of the acquisition of shares in GENELEC by CHABRIAS, the Calcutta Stock Exchange protested the deal. In spite of the strong and genuine protests of Calcutta Stock Exchange, the Government could not come to the rescue of the minority shareholders. Further he explains that clause 40 does not have the force of a statutory law and is very often circumvented by intelligent bulk purchasers by keeping the percentage of shares acquired by them within the prescribed provisions of the listing agreement and yet, at the same time achieving the object of getting an unquestionable controlling interest in the corporate Company.

In such cases even a small block of shares can make the purchaser of even less than 20 percent the eventual owner.

The basic problem with 40-A is that it relates only to Individuals (the earlier Rule-40 dealt with both individuals and Groups). As a result, a raider could get around the
situation by having a number of intermediaries holding shares for him and all below 5 per cent. Also, in many companies, the holdings of the financial institutions are very large.

In the case of merger the interests of the shareholders of amalgamating company and the shareholders of amalgamated company are effected. If a sick company is merged with the healthy company the shareholders of the sick company will exchange their shares with the healthy company in the proportion already decided. In this scheme the sick company shareholders stand to gain by receiving their dividends and their shares can be marketed in the stock exchange without any difficulty. The shareholders of the healthy company will have to share their prosperity along with the new shareholders. The plight of this type of shareholders is explained by Professor S D BALSARA, former Dean of Faculty of Law, Bombay University in his article on "AMALGAMATION SCHEMES" SHAREHOLDERS, BEWARE!" (FORTUNE INDIA 43, October 1988).

The scheme of amalgamation between Neomer Limited and Alembic Chemical Works Limited was approved by the Central Government under the Monopolies and Restrictive Trade Practices Act. It was also approved by a majority of shareholders, depositors, debenture holders and secured creditors.
However, one shareholder who was also Secretary of the Workers Union of Alembic Chemical Works Limited, rejected on the following grounds:-

1) Neomer's history showed that it was never a financially viable unit.

2) The report of the Chartered Accountants had not taken into consideration certain relevant factors and it did not indicate as to how the break-up value of Neomer's shares had been carried out at about Rs.5/- per share. Further Alembic was required to take over the liability of paying dividends and writing off of loans of Neomer.

3) The Directors of Alembic collected proxies from employees.

4) Apart from material non-disclosure in the explanatory statement, at the meeting of Alembic's shareholders, the scheme did not show any tangible benefit to Alembic by the proposed amalgamation.

5) As per the proposed scheme, the shareholders of Neomer would be getting dividends from 1983 as effective date of amalgamation was from 1983. But as Neomer never made any profits, how could the shareholders get any benefit?

The Gujarat High Court rejected all the objections on the following grounds:
1) The scheme ought to be sanctioned because an overwhelming majority of creditors and shareholders at their meetings sanctioned the scheme. Further, it was also sanctioned by the MRTP and Income Tax authorities.

2) The break-up value of Neomer's shares could not be regarded as grossly exaggerated, as these shares were quoted on the stock market at about Rs.5/-.

3) The Neomer shareholders were made members of Alembic from 1983, the effective date of amalgamation. Once the amalgamation scheme was sanctioned, it would relate back to the effective date. Hence the shareholders would be entitled to all the benefits (as well as liabilities, if any) of ALEMBIC.

The aggrieved shareholders put forward the same directions to the Appellate Court, but the appeal was rejected. (Jitendra R Sukhadia Vs Alembic Chemical Works Company Limited, 1988 64 Comp CAS 206).

Professor S D Balsara feels that the shareholders of ALEMBIC CHEMICAL WORKS LIMITED were taken for a ride and the pity is that the shareholders were willing parties to the disadvantage they were put in. What benefit can the shareholders derive from supporting a proved sick unit with no prospect of success? Despite Neomer making losses, Alembic took over its liabilities which were far in excess of its assets. Was Alembic not planning to revive Neomer's Plants? His suspicion is based on the trial Court's order that the Alembic shall not close down the Neomer's Unit which now stands transferred to it, for a period of 10 years.
except in accordance with Law. Hence, in course of time, Alembic may close down Neomer's unit as being not viable. Further, a close down can only be in accordance with Law and no Law prohibits a unit which is continuously making losses from being closed down.

This case reiterates the minority shareholders' opinion that individual shareholders are not able to protect their interests. The only way it can be done is by forming strong Shareholders Associations, which should have representation at Ordinary General Meetings of Companies, as suggested by the SACHAR COMMISSION.