Corporate Conquest: Analysing Hostile Takeovers and their Impact on Organizational Dynamics

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Abstract:
While the merger and acquisition (“M&A”) activity in India was largely resilient during the period 2015-2019, India witnessed a surge with deal values in 2022 where strategic M&A deal volume and value reached all-time highs in India, while deal-making dropped off in much of the rest of the world.¹ M&A in India was boosted by more than 20 large transactions and reached a record high of USD 107 billion — almost twice that of 2021². One of the largest M&A was the merger of HDFC with HDFC Bank with the deal value pegged at USD 60 Billion which was the biggest in India’s corporate history and was higher than the total value of all deals — USD 52 Billion in 2021. 2022 witnessed some of the largest-ever transactions in the cement, aviation and banking sectors, which were driven by companies looking to either consolidate their positions or enter new segments. Although deal activity in 2022 has been lower than 2021, it has surpassed pre-pandemic levels. The general M&A activity in India is near an all-time high with more companies are doing more deals than ever before.³ Hostile takeovers make up 19% of all mergers and acquisitions worldwide, and they are at an all-time high as businesses with robust balance sheets continue to buy out their less strong competitors for a small portion of their actual worth. This paper aims to bring in the analysis of Hostile takeovers and their impact on organizational dynamics with specific references to the provisions of Companies Act, 2013 and the Regulation of takeover by SEBI in India.

Keywords: Hostile takeover, Merger, acquisition, Target Company, Takeover code.

Introduction:
A hostile takeover refers to the acquisition of a target company by another entity (the acquiring company) against the wishes of the target company's management and board of directors. Unlike a friendly takeover, where the target company's leadership is in agreement with the acquisition and supports the process, a hostile takeover involves a more confrontational approach. India, with its diverse and robust business environment, has witnessed several instances of hostile takeovers that have garnered attention both nationally and globally. The regulatory framework surrounding takeovers in India is primarily governed by the Securities and Exchange Board of India (SEBI), which has laid down stringent rules and guidelines under the Takeover Code to ensure transparency, fairness, and the protection of shareholder interests.

¹ https://www.bain.com/insights/india-m-and-a-report-2023/
² PwC India report, titled ‘Deals in India: Annual Review 2022’
³ Nishithdesai.com
Research objectives:
1. To examine the Indian legal and regulatory frameworks that are currently in place regarding takeovers.
2. To evaluate Indian regulatory agencies that monitor and address hostile takeover-related issues.
3. To analyze and make inferences from case studies of prominent hostile takeovers in India.

Research methodology:
This paper's information was gathered from a number of websites, journals, and research papers. This study is descriptive in nature and uses a qualitative approach. Given that it offers a comprehensive summary of the topic and the problem, it takes a broader descriptive approach. This work was produced without using or gathering any primary data. No primary sources are used in this paper.

Regulatory Frameworks:
The "Companies Act, 2013" is the main piece of legislation that governs companies in India. This act provides the framework for laws pertaining to corporate governance, mergers, acquisitions, and takeovers. Plans of arrangement between a business, its shareholders, and creditors are governed by the Merger Provisions. The Merger Provisions are actually written so broadly that they cover and govern every possible corporate restructuring that a business may engage in, including spin-offs and hive-offs, mergers, amalgamations, demergers, and any other type of compromise, settlement, agreement, or arrangement between a business and its shareholders or creditors.

I. Share Transferability:
In general, an Indian business can be established as either a public or private company. A private company's articles of association, or byelaws, contain inherent restrictions on the transferability of its shares. These restrictions typically take the form of a pre-emptive right that favour the other shareholders. Even though a public company's shares are freely transferable, share transfer restrictions have been granted statutory sanction with the introduction of CA 2013. Certain share transfer procedures may be specified in the articles of association and must be followed in order to complete a share transfer.

II. Squeeze out Clauses:
1. Companies Act, 2013 Section 236:
A public company may refuse to register a share transfer under Section 58(4) of the CA 2013 for a "sufficient cause" if a person or group of people acquires 90% or more of the company's shares through an amalgamation, share exchange, conversion of securities, or for any other reason. In addition to notifying the company of their intention to purchase the remaining equity shares of the company, the person(s) in question shall have the following additional requirements. Section 236 of the CA 2013 states that if a person or group of people acquires 90% or Specific considerations when shares of an Indian company are acquired by a non-Indian acquirer a right to make an offer to buy out minority shareholders at a price determined by a registered valuer, which price shall be determined based on the fair value of the company's shares after taking into account valuation parameters such as return on net worth, book value of shares, earnings per share, price earning multiple vis-a-vis the industry average, and such other parameters as are customary for valuation of such companies' shares.
2. Companies Act, 2013 Section 230:
Following the filing of an application for compromise or arrangement before the NCLT, shareholders of unlisted companies holding at least 75% of the securities (including depository receipts) with voting rights may make an offer to purchase all or a portion of the remaining shares of the company. This is permitted by 2013 Section 230 read in conjunction with Rule 3 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016, which went into effect on February 7, 2020. Minority shareholders would be compelled to sell their shares to the acquiring shareholder as soon as NCLT approved the acquisition offer. Only unlisted companies are eligible to use this squeeze-out technique, and listed companies must abide by the rules set forth by SEBI in this regard.

3. Companies Act, 2013 Section 186:
The CA 2013 sets limits on loans and investments between corporations in Section 186. An Indian company that wishes to acquire securities from another body corporate may do so by subscription, purchase, or other means up to (i) 60% of the acquirer's paid-up share capital, free reserves, and securities premium, or (ii) 100% of its free reserves plus the securities premium account, the greater of the two. But the acquirer is allowed to purchase more shares than these, provided its shareholders approve it through a special resolution adopted during a general assembly. These restrictions do not apply when making a purchase of a fully owned subsidiary's securities.

4. Companies Act, 2013 Section 235:
This section pertains to businesses that wish to purchase another business's shares. It is important to note that members who hold ninety percent of the target company's shares are required to vote in favour of the resolution approving the scheme of arrangement, even though the section does not specify a specific share threshold restriction.

The SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (the “Takeover Code”)
The acquisition of shares and takeovers of publicly traded companies in India are governed by SEBI regulations. Essentially, the regulations set up thresholds for acquisitions above which the acquirer is required to present an open offer to the shareholders. The regulations cover the purchase of management control, voluntary offers, share delisting, acquisition pricing standards, related disclosures, and the specific responsibilities of the target and acquirer. Some of the important provisions are:
Regulation 3(1) states that when an acquirer obtains more than 25% of a target's shares or voting rights, it is considered a large acquisition and necessitates an open offer. When an outsider or non-shareholder acquires shares for the first time, this is referred to as the acquirer crossing the trigger point. The regulations outlined in Reg. 3(2) also apply to the consolidation of shares held by members who hold a 25% or greater stake in the company or voting rights. This is applicable to any purchase of 25% to 75% of the target's shares or voting rights. In these cases, an open offer must be made each time the acquirer acquires more than 5%.
Regulation 4 - This provision applies to the acquisition of control, either with or without the acquisition of shares, and would typically involve the powers to appoint a new board of directors.
Regulation 6 - This provision has made voluntary open offers by outsiders almost impossible, as people with a minimum of 25% shareholding in the company can make voluntary open offers. Furthermore, rules
such as not acquiring shares in the target firm for 52 weeks before, during, and after the acquisition of control have made voluntary open offers by outsider
Reg. 26 - This clause imposes a number of duties on the target business, including:

- Alienation from the company during the offer period, including any material assets
- Taking out any significant loans or borrowings
- The issuance or distribution of shares
- Repurchasing of shares
- Signing or cancelling any significant contracts
- Quickening of rights such as Employee Stock Options (ESOPs) contingent vesting

Hostile Takeovers in India:
In the Indian market, hostile takeovers are not commonplace. The following lists some of the most prominent hostile takeover cases from both India and overseas.

1. Adani groups takeover of NDTV:
The richest man in Asia, Adani, began a hostile takeover of media behemoth NDTV by first indirectly acquiring a 29.18% stake in the broadcaster and then making a bid to purchase a 26% controlling stake. According to NDTV, neither the company nor the founders had any say in the conversion of the debt into equity. Acquisition of the remaining 29.18% of NDTV occurred without "discussion, consent or notice". Adani Enterprises paid ₹602 crore to NDTV promoters Radhika and Prannoy Roy for an additional 1.76 crore shares of the network through its indirect subsidiary RRPR Holdings. This translated into a 27.26% ownership position in the business.

2. India cements takeover of Raasi cements:
The sale of BV Raju's 32% share in Raasi Cements to India Cements in 1998 is a prime example of a hostile takeover in the Indian business sector, which ultimately led to the tragedy's acquisition by an adversarial bidder. India Cements Limited, which already owned 9.75% of Raasi Cements, acquired an additional 8.28% on a spot basis from a specific group of Raasi Cements' promoters, triggering the open offer under the previous takeover regime. The purchase was rejected by Raasi Cements' surviving supporters. Following a fruitless legal battle and the inability to generate a counter proposal, Raasi Cement's promoters ultimately consented to sell India Cements their 32% stake. India Cements acquired full control of Raasi Cements through an open offer of 20% and the acquisition of the promoter group's entire stake.

3. Acquisition of Mindtree and L&T
Following India Cement's successful acquisition of Raasi Cement, this was the second takeover of that kind. In 2019, Larsen and Toubro Ltd. (L&T) acquired a majority position in Mindtree Ltd., increasing its ownership to 60% of the Bengaluru-based business. As major investors hurried to sell their holdings, L&T completed acquiring the 31% additional stake in Mindtree that it had targeted for ₹4,988.82 crore through an open offer. L&T has total control over the board and management of the software company Mindtree thanks to its 60% ownership.
The culmination of a year-long endeavour by the Mumbai-based engineering behemoth to acquire control of Mindtree through a hostile bid was the purchase of additional shares by L&T through an open offer
following the acquisition of a 20.4% stake in the company from coffee baron VG Siddhartha and affiliate firms.

**Ethical and Legal challenges:**
Hostile takeovers, characterized by the acquisition of a company against the wishes of its management, present numerous ethical and legal challenges in India. These challenges arise from the clash between the acquirer's pursuit of financial gains and the potential negative impact on stakeholders, as well as the need to adhere to India's regulatory framework.

**Ethical Challenges:**
1. **Stakeholder Interests:**
   Hostile takeovers often prioritize the interests of the acquiring company and its shareholders over those of the target company's stakeholders, including employees, suppliers, and local communities. This raises ethical concerns about the impact on livelihoods and the broader community.

2. **Employee Welfare:**
   Employees of the target company may face uncertainty and job insecurity during a hostile takeover. Ethical questions arise about how the acquiring company handles workforce integration, layoffs, and ensuring a fair transition for employees.

3. **Corporate Governance:**
   Hostile takeovers can strain principles of good corporate governance. The acquiring company might bypass existing management structures, potentially leading to a decline in transparency, accountability, and overall governance standards.

4. **Cultural Integration:**
   Mergers and acquisitions often involve a clash of corporate cultures. Hostile takeovers may amplify these challenges, as there is little room for pre-deal negotiations to address cultural differences, potentially leading to ethical dilemmas in managing a cohesive work environment.

5. **Legal Challenges:**
   1. **Regulatory Compliance:**
      India has stringent regulations governing mergers and acquisitions to protect the interests of stakeholders. Hostile takeovers may face legal challenges if the acquiring company does not adhere to these regulations, leading to scrutiny from regulatory bodies.

   2. **Takeover Code:**
      The Securities and Exchange Board of India (SEBI) has laid down the Takeover Code, which sets out the rules and regulations for acquiring control over public-listed companies. Hostile takeovers must comply with these regulations, including making mandatory open offers to the existing shareholders.

   3. **Minority Shareholder Rights:**
      Hostile takeovers may raise concerns about protecting the rights of minority shareholders. The acquirer must ensure that minority shareholders are treated fairly and are provided with an opportunity to exit at a reasonable price.
4. **Antitrust Laws:**
Antitrust regulations are designed to prevent monopolistic practices and ensure fair competition. Hostile takeovers that lead to market dominance may face legal challenges under India's competition laws.

5. **Contractual Obligations:**
The acquiring company may face legal hurdles if it breaches existing contractual obligations of the target company. These could include agreements with suppliers, customers, or other stakeholders, and violating these contracts may lead to legal consequences.

**Judicial pronouncements:**

1. **Pramod Jain And Ors vs Sebi**
The Supreme Court in this case observed that "An acquisition of a company's controlling interest may be amicable or hostile. The target company's management sells the acquirer its majority stake in a friendly acquisition. An acquirer may directly approach shareholders with an open offer, known as a hostile takeover, if the target company's management is unwilling to engage in negotiations. A hostile takeover enables the shares' hidden value to be discovered and puts pressure on the management to perform well. Alternatively, it may unnecessarily disrupt the regular operations of a target company. Therefore, in the post-liberalization era following 1991, there is an indisputable need to regulate the process of acquisition and takeovers. It is common knowledge that defense tactics like "Poison Pills," which make an acquisition unfeasible for the acquirer by raising the cost of acquisition, "Shark Repellents," which take steps to thwart an unwanted takeover, the sale of valuable assets, etc., are used when a takeover attempt proves unpleasant for the target company.

**Legal safeguards and mechanisms:**
Indian corporate law renders ineffective traditional takeover defenses like the poison pill and staggered board, leaving target companies with limited options to repel hostile bids. Due to a lack of takeover defenses, Indian companies are in a risky position as a result of the government's recent laws permitting foreign hostile takeovers.

A. **Poison Pills:** Also referred to as the shareholders' right plan, a poison pill strategy involves the target company diluting its shares until the acquirer is unable to obtain a controlling position without incurring large expenses. Using this method, the company issues securities that contain restricted rights that can only be used in response to a certain set of circumstances. If a 20% acquisition, for example, triggers the additional shares, existing shareholders will have a special right to buy them at a reduced price. Although this tactic frequently resulted in losses for the targeted company, it was occasionally quite successful in preventing a hostile takeover. Netflix banished the acquirer by using a poison pill.
When Saurashtra Cement distributed shares to its promoter and other foreign businesses

B. **The White Knight:** Should the board of the target company feel it will be unable to prevent a hostile takeover, it may search for a more amiable company to purchase a controlling stake in the business before the hostile bidder does.
GESCO employed the same strategy to protect Renaissance Real Estate, with Mahindra and Mahindra acting as the white knights.
C. Pac Man Defense: In an attempt to protect itself, the target company switches roles, offers a counteroffer to the acquirer, purchases shares in the acquiring business, and threatens to buy the raider outright. The raider consequently becomes obsessed with preserving itself, which compels them to come to a compromise.

D. Greenmail: This tactic involves the target company paying a premium for its own stock that it repurchases from the acquirer. The SEBI Listing Obligations and Disclosure Requirements (LODR) Regulations, 2015, specifically Regulations 29(1) (b) and 29(2), mandate that management provide notice prior to contemplating a share buyback.

E. Crown Jewels: By selling off its most valuable asset—which might have drawn the acquirer in the first place—the target lessens its appeal to the buyer. Using this strategy in tandem with a white knight, the target company would demerge its valuable asset and sell it to the knight, who would later purchase it back at a predetermined price. A company cannot sell its venture without the prior approval of shareholders as per section 180 of the companies Act.

Conclusion:
In conclusion, the research on hostile takeovers illuminates a landscape where financial gains intersect with ethical and legal challenges. Striking a balance between shareholder interests and stakeholder well-being is crucial. India's regulatory framework, including the Takeover Code and antitrust laws, offers legal safeguards, emphasizing compliance and protecting minority shareholders. Moving forward, corporations must prioritize ethical considerations alongside financial objectives, fostering a culture of transparency and responsibility in the face of hostile takeovers for sustainable and socially responsible business practices.