

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

IN THE MATTER OF ACQUISITION OF SHARES BY STERLING INVESTMENT CORPORATION PRIVATE LIMITED, SHAPOORJI PALLONJI AND COMPANY LIMITED AND CYRUS INVESTMENTS LIMITED IN M/S FAL INDUSTRIES LIMITED

WTMN/195 /CFD/8/04

BACKGROUND:

- 1.1 Sterling Investment Corporation P Ltd. (Sterling), Shapoorji Pallonji and Company Ltd. (SPCL) and Cyrus Investments Ltd (CIL) (collectively referred to as the acquirers) made an open offer in terms of Regulation 10 read with Regulation 12 of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (hereinafter referred to as the Regulations) to the shareholders of Forbes Gokak Ltd., a listed company (for brevity's sake referred to as FGL). The said offer opened on November 28, 2001 and closed on January 10, 2002. Sterling and CIL are subsidiaries of SPCL, and together referred to as the Shapoorji group. Prior to the said offer, as per the disclosures made in the letter of offer dated November 23, 2001, the acquirers were stated to be holding 14.89% in FGL. The post offer shareholding of the acquirers as per the 45 day report submitted by the merchant banker was 67.57%.
- 1.2 At the time of making the public announcement, FGL, its subsidiary Forbes Estate Limited (FEL) and Warrior (Investments) Limited (WIL) were respectively holding 31.64%, 5.8% & 0.24% and collectively 37.68% shares in FAL Industries Limited [for brevity's sake hereinafter referred to as FIL (target company)]. The Tata group comprising of Sabras Invest and Trading Co Ltd., Bambino Invest and Trading Co Ltd and Tata Investment Corporation was collectively holding 20.65% paid up equity share capital in FIL. FGL along with the Tata Group were in the aggregate holding 58.35% of the equity share capital of FIL and shown as the promoter group for the years 2000 and 2001.
- 1.3 The Securities and Exchange Board of India (hereinafter referred to as the SEBI) received a complaint to the effect that the non-promoter shareholding of FIL had increased from 41.67% as on 31/3/2001 to 62.32% as on 31/12/2001 and that as on 31/3/2002, it was 60.76%. On the said basis, it was alleged that someone had probably acquired more than 20% shares.
- 1.4 On taking up the matter with the target company, the following facts emerged:
- Prior to the above-mentioned offer, FGL was under the control of entities belonging to the Tata group which held 14.83% of its shareholding, while the Shapoorji group for many years held 8% of its shareholding. Pursuant to a restructuring in the shareholding pattern of FGL, the Tata group sold its 14.83% shareholding in FGL to the Shapoorji group which necessitated the open offer and consequently the post offer shareholding of the acquirers in FGL as per the 45 day report submitted by the merchant banker was 67.57%.
- 1.5 The disclosures made under Regulation. 8 of the Regulations by FGL to Target Company for the year ended 31.3.2002 revealed FGL and the Tata group as promoters and the acquirers as the public. However the disclosures made in June 2002, after the open offer for FGL, in terms of Regulation 8 of the Regulations disclosed the acquirers in the promoters' category along with FGL while the Tata group were shown in the public category.
- 1.6 Prior to the open offer in FGL, FGL along with the Tata Group seemed to have been in control of the Target Company and shown as the promoter group. Subsequent to the change in control of FGL, when the Tata Group sold their stake and the Shapoorji group acquired control over FGL, there was a change in control in FIL as well, when only FGL along with 2 new entities - Sterling and Shapoorji were shown under the head "promoters". Considering the above, it was observed that acquirers ought to have made an open offer for FIL when they made an offer for the shareholders of FGL on October 15, 2001, as consequent to their acquiring control over FGL, they also acquired control over FIL.

SHOW CAUSE NOTICE AND REPLY:

- 2.1 A show cause notice dated May 29, 2003 was issued to the acquirers to show cause as to why one or more or all action(s) under Regulation 44 and Regulation 45 of the Regulations and Sections 11, 11B, 15H and 24 of the SEBI Act, should not be initiated against them for failing to make a public announcement to acquire the shares of FIL as required by the provisions of Regulations resulting in the violation of the provisions of Regulations 10 & 12 read with 14(1) & 14 (3) of the Regulations.
- 2.2 In reply to the same, the acquirers vide their letter dated June 30, 2003, contended, inter alia that the acquirers along with their subsidiary, i.e. FGL had a collective shareholding of 39.24% only in FIL which could not give them controlling interest and hence the acquirers could not have acquired control of FIL as contemplated in Regulation 12 read with Regulation 2(1) (c) of the Regulations. The acquirers stated that FIL, incorporated on 26 October 1962, was jointly promoted by Facit AB of Sweden and Forbes Forbes Campbell & Co. Ltd. ("FFCCL"). Since FFCCL one of the promoters of FIL (earlier known as Facit Asia Ltd) merged with FGL in 1992. FGL was regarded as a promoter of FIL, in the initial equity capital, FFCCL had been allotted 3000 equity shares of Rs.100/- each i.e. 10% of the initial equity capital of FIL. It was contended that while in or

about 1992, FFCCL merged with FGL, Facit AB, Sweden which held 25.74% was accorded approval by the Reserve Bank of India under the provisions of the FERA 1973 to divest its aforesaid holding to two investment companies; Forbes Campbell Holdings Ltd (FCHL) (7,52,000 shares) and WIL (30,555 shares) to redinvest in favour of Indian shareholders. Since FGL held 49% of equity capital of WIL, FGL was instrumental in the formulation of offer for sale document by which shares held by FCHL and WIL came to be offered to the public. In the offer for sale document dated 25th January 1994, issued by FCHL and WIL, Forbes was shown as a major shareholder, holding 23.24% equity in FIL, which would imply that FGL was a promoter of FIL. It was stated that in this background, FGL was disclosed as a promoter of FIL in the letter dated 17.4.2002 addressed by FGL to FIL. Therefore, Sterling was shown as a part of promoters' group in terms of Regulation 2(1)(h)(3)(i). Similarly, SPCL being holding Company of Sterling was also included as a promoter by virtue of the aforesaid Regulations.

- 2.3 The acquirers also contended that the violation, if any of Regulation 10 and/or Regulation 12 was technical in nature in view of the difficulties of interpretation of the Regulations and due to a bonafide belief that they were not required to make a public offer for the shares of FIL and also their contention that they had not acted deliberately in defiance of law or in conscious disregard of their obligations and had not made any gain or unfair advantage nor had they caused any loss to any one, and the default, if any, was not of a repetitive nature and thus there was no "mens rea" on their part and hence having regard to the fact that they had not committed any default in the past, no proceedings ought to have been initiated against them.

HEARING

- 3.1 Thereafter, upon their request, the acquirers were granted a personal hearing on May 27, 2004. when Mr Janak Dwarkadas, Senior Counsel, Mr P.N Kapadia and Ms Ayesha Cooper from Gagrut & Co, Mr J.J Parekh and Mr A.T. Shah appeared on behalf of the acquirers and reiterated the submissions made earlier. It was further contended that neither Sterling nor SPCL nor CIL nor all of them together had the power to appoint the majority of the directors of FIL nor could they control nor have they controlled the management or policy decisions of FIL, whether on their own or in concert directly or indirectly with others, whether by virtue of the shareholding or management rights or shareholders agreement or voting agreements or in any other manner and had no agreement with any party for management rights of FIL nor had they any voting agreement or shareholders agreement in respect of voting in FIL and as such could not have said to have acquired control of FIL as contemplated in Regulation 12 read with Regulation 2(1)(c) of the Regulations.

CONSIDERATION OF ISSUES

- 4.1 I have taken into consideration the facts and circumstances of the case and the material available on record which includes the show cause notice and the reply of the parties to the same.
- 4.2 I have perused the disclosures made under Regulation 8(2) of the Regulations by FGL to FIL. Further I have also noted the disclosures made by FIL to the stock exchanges in terms of Regulation 8(3) wherein the list of shareholders "who have control over the company" i.e. the promoter group has been declared. The same includes the names of FGL, FEL, WIL and the Tata Group companies.
- 4.3 It is noted that for the years 2000 and 2001, FGL along with the Tata Group were in control of FAL and were shown as the promoter group, before the open offer made in relation to the acquisition in FGL. Subsequent to the change in control of FGL, when the Tata Group sold their stake and the Shapoorji group acquired control over FGL, there was a change in control in FAL as well, when only FGL along with 2 new entities - Sterling and Shapoorji were shown under the head "promoters".
- 4.4 I have noted that in the annual report of FGL for the years 2000-01 and 2001-02, target company has been disclosed as an "associate company" of FGL. Further page 21 of the annual report of FGL for the year 2001-02 discloses FGL as a subsidiary of the Shapoorji Pallonji group pursuant to the open offer made by the acquirers for the shares of FGL. Further, the disclosures made in June 2002, in terms of Regulation 8 of the Regulations after the open offer for FGL, show the acquirers in the promoters' category along with FGL, while the Tata group are shown in the public category. The said position has been acknowledged even by FIL, vide their letter dated September 17, 2002.
- 4.5 FGL along with FEL and WIL had been declared to be in control over FIL in years prior to open offer made and were running the management of FIL, along with the Tata Group. However, pursuant to the acquirers' acquiring control over FGL from the Tata Group, the Tata Group lost control over FIL as well and FGL along with its holding company, Sterling became the controlling group over FIL.
- 4.6 As per the list of directors on the Board of FIL at the time of the public announcement made by the acquirers for the shares of FGL, the Chairman of the Board of Directors of FIL was also the Deputy Chairman and Managing Director of FGL and that one of the Non Executive Directors of FIL was the Executive Director (Finance) of FGL.
- 4.7 The said positions on the Board of the company by representatives of FGL would enable the acquirers, being the controlling body over FGL, to indirectly influence or control any business or policy decisions taken by the management of the company.

- 4.8 Moreover the contention of the acquirers that they do not have, directly or indirectly, by virtue of any shareholding or management rights or shareholders agreement or voting rights, control or the right to appoint the majority of directors of FIL, appears to be unsustainable in that in terms of the provisions of the Regulations, the definition of "control" does not intend to bring, within its ambit, only the written agreements.
- 4.9 The fact remains that there has been an indirect acquisition of shares of FIL in the present case in that although FGL had earlier to the offer been declared to be in control over FIL under Regulation 8 of the Regulations, pursuant to the open offer made by the acquirers for acquiring the shares of FGL and subsequent purchases made during the offer period, the acquirers' shareholding in FGL became 69.67% and hence the acquirers were shown as a promoter in 2002 in the disclosures made under Regulation 8 of the Regulations as they had also acquired control over FIL. The same has been disclosed in the Annual Report of FGL for the year 2001-2002, wherein FGL is shown as a subsidiary company of SPCL (one of the acquirers). The fact also remains that prior to the aforesaid open offer by the acquirers for acquisition of the shares in FGL, FGL were holding 31.64% in FIL. Further, FEL and WIL were holding 5.80% and 0.24% respectively in FIL. Thus their collective shareholding was 37.68% in FIL. However when the acquirers acquired control over FGL, it indirectly acquired control over the said 31.64% shares held by its subsidiary i.e, FGL in FIL. Therefore, Regulation 10 of the Regulations was attracted as regards indirect acquisition of 31.64% shares in FIL and from the facts stated above, it is established that Regulation 12 of the Regulations was also attracted.
- 4.10 Disclosures under Regulation 8 of the Regulations have a special significance attached to them in that the said disclosures are intended to disclose timely information to the target company and the public shareholders as to the identity of the persons/ group that are promoters/in control over a particular target company. It is with this intention in mind that the promoters of the promoters have also been covered in the definition of promoters with respect to a target company. In view of the above, the contention of the acquirers that they did not acquire control over the target company appears to be contradictory in nature vis-à-vis their own disclosure to the target company/ target company's disclosure to the stock exchanges.
- 4.11 The acquirers have also contended that by no stretch of imagination could FGL be termed as the holding company of FIL. In this regard it would be relevant to note the observations contained in the Report of the Bhagwati Committee. The Committee observed that acquisition of an unlisted company would not be exempted if by virtue of such acquisition, or change in control of the unlisted company whether in India or abroad, a change is brought about in the control of the listed company or acquisition of control over the voting rights of the listed company in as much as occasionally, a person or group of persons acquiring statutory control of a company (which need not be a company to which the Regulations apply) thereby acquire control of a second company because the first company itself holds a controlling block of shares in the second company, or holds shares which, when aggregated with those already held by the person or group, secure or consolidate control of the second company. The said concept has been incorporated in the present amended Regulations. Similarly the cases where a person or group of persons acquire statutory control of a company (which need not be a company to which the Regulations apply) and thereby acquire control of a second company because the first company itself holds a controlling block of shares in the second company, or holds shares which, when aggregated with those already held by the person or group, secure or consolidate control of the second company, have also been brought within the ambit of the Regulations.
- 4.12 It is thus seen that the Regulations intended to bring within its ambit such acquisitions as described above, and hence the indirect acquisition of shares and control over FIL by the acquirers can be stated to be covered under the aforesaid type of acquisitions and therefore the provisions of the Regulations would be applicable in the instant case.
- 4.13 It is thus clear that when the acquirers made the public announcement on October 15, 2001 in terms of Regulations 10 and 12 of the Regulations to acquire shares of FGL, they not only decided to acquire shares/ voting rights/ control over FGL but also decided to acquire shares/ voting rights/ control indirectly over target company. Therefore, they should have made a public announcement to acquire shares/ voting rights/ control to the shareholders of FIL also in terms of Regulations 10 and 12 of the Regulations on October 15, 2001.
- 4.14 I have noted that despite their stand the acquirers did make a public announcement on October 11, 2003 to acquire 20% of the shares of FIL, too. According to the draft letter of offer submitted to SEBI, the acquirers had made the public announcement, by way of "abundant caution" in the wake of issuance of the show cause notice by SEBI. Furthermore, the said public announcement was described as "voluntary" in nature. The said offer opened on January 22, 2004 and closed on February 20, 2004. While the offer was open, the merchant banker to the offer informed SEBI that the acquirers had purchased 9,41,286 shares (20.65%) of FIL from the Tata Group on February 6, 2004. As per the 45 day report with reference to the final status and the post offer shareholding of the acquirers, it is noted that the post offer shareholding of the acquirers stood at 78.63% and the balance 21.37% being with the public.

CONCLUSION:

- 5.1 The facts and circumstances of the case lead to reasonable conclusion that consequent on acquiring of control of FGL, the acquirers namely Sterling Investment Corporation P Ltd, Shapoorji Pallonji and Company Ltd and Cyrus Investments Ltd acquired control over FAL Industries Ltd. (FIL) as well. It is noted that notwithstanding the fact that acquirers were contesting the allegations contained in the show cause notice issued by SEBI for violation of Takeover Regulations, the acquirers have since "voluntarily" made

open offer for acquiring shares from the public in accordance with the Regulations on October 11, 2003 and the price offered for the shares to be acquired has been determined reckoning interest from October 15, 2001 taken as reference date for calculation of the offer price. Thus, the acquirers have complied with the regulatory requirement in so far as it relates to public announcement for acquiring shares from the public consequent on acquiring control over FIL. However, the said public offer ought to have been made within the time specified in the Regulations. It was only after issuance of show cause notice and initiation of regulatory proceedings by SEBI that the acquirers have made the open offer to the shareholders of FIL. In the process, the open offer has been made after almost 2 years of delay. It can be reasonably inferred that but for the show cause notice issued by SEBI, the acquirers would not have made the public offer. In the circumstances, the delay in compliance with the regulatory requirement needs to be appropriately dealt with. I, therefore, consider it fit to refer the case for adjudication proceedings under section 15H of the SEBI Act for delay in compliance with provisions of regulation 10 and 12 read with Regulation 14(1) and 14(3) of the Takeover Regulations. The order for appointment of adjudication officer in this regard will be issued separately.

5.2 In view of the above, I, in exercise of the powers conferred upon me under Section 19 and Sections 11 and 11B of the Securities and Exchange Board of India Act, 1992 read with Regulations 44 and 45 of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997, hereby direct that the matter of delay in compliance with provisions of the Takeover Regulations on the part of Sterling Investment Corporation P Ltd, Shapoorji Pallonji and Company Ltd and Cyrus Investments Ltd. be referred to adjudication.

T.M. NAGARAJAN

Date : August 31, 2004

WHOLE TIME MEMBER

Place: Mumbai

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