

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

IN THE MATTER OF ACQUISITION OF SHARES & CHANGE IN CONTROL OF BIHAR CAUSTIC & CHEMICALS LTD. THROUGH RIGHTS ISSUE BY HINDALCO INDUSTRIES LTD. AND PILANI INVESTMENT AND INDUSTRIES CORPORATION LTD. -- VIOLATION OF REGULATIONS 11(1) AND 12 READ WITH 14(1) AND 14(3) OF THE SEBI (SUBSTANTIAL ACQUISITION OF SHARES AND TAKEOVERS) REGULATIONS, 1997 – DIRECTIONS UNDER REGULATIONS 44 (f) & (i) OF SEBI (SAST) REGULATIONS 1997 TO HINDALCO INDUSTRIES LTD. AND PILANI INVESTMENTS CORPORATION LTD.

1.0 BACKGROUND

- 1.1 Bihar Caustic and Chemicals Ltd (hereinafter referred to as Target Company), incorporated on July 20, 1976, is a company having its shares listed on BSE, CSE and DSE. Bihar State Industrial Development Corporation Ltd (BSIDCL) and Birla group companies viz., Hindalco Industries Ltd (HIL) along with Pilani Investments Corporation Ltd. (hereinafter referred to as the Acquirers) and Grasim promoted the Target Company. The Target Company was controlled by the aforesaid parties as per their Joint Venture agreement (J V Agreement) dated June 12, 1976. The J V agreement governed the rights of the Acquirers and BSIDCL in respect of the management of the Target Company. Originally, BSIDCL and Birla Group companies were holding 26% and 25% respectively.
- 1.2 The JV agreement was renewed / extended from time to time until the last extension dated June 27, 1998 and in accordance with the same, the J V Agreement lapsed on or about June 11, 2002. Thereafter, neither of the parties took any steps for its renewal.
- 1.3 In February 2003, the Target Company offered further equity shares in the Company by way of a rights issue to the existing shareholders. The offer was contained in the Letter of Offer dated January 30, 2003. The rights issue was proposed in order to raise Rs.15.6 crores of equity capital to part-finance the setting up of a 30-MW coal based power plant adjacent to its existing caustic soda unit at Garhwa Road, Jharkhand.
- 1.4 The Board of Directors of the Target Company while authorizing the rights issue vide resolution dated March 20, 2002 provided that the promoter shareholders should confirm to the company at least ten days before the closure of the rights issue whether they will subscribe to their share of the rights issue or other promoter/third party shall subscribe to their share of rights shares. BSIDCL decided not to subscribe to the rights issue. It was therefore disclosed in the Letter of Offer that BSIDCL, by its letter of July 1, 2002 informed the Target Company that the Government of Bihar had intimated to BSIDCL that it "will not be proper to invest further" by the Government of Bihar/BSIDCL in the Company. HIL by its letter dated June 18, 2002 undertook that it will subscribe to its rights entitlement in full, and in addition it intends to apply for additional shares to the extent the issue was undersubscribed. It was further stated that such acquisition of shares, if allotted to HIL would be in accordance with the provisions of Regulation 3(1)(b) of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 (hereinafter referred to as the Regulations) and will therefore be exempt from the applicability of Regulations 11 and 12 of the Regulations.
- 1.5 On May 7, 2003, shares were allotted pursuant to the rights issue. The shareholding of the Target Company before and after the rights issue is as follows:

Shareholder	Pre-Rights Issue		Post Rights Issue	
	No. of Shares	Percentage	No. of Shares	Percentage
BSIDCL	20,28,000	26%	20,28,000	8.67%
HIL	15,60,000	20%	1,27,62,287	54.57%
Pilani	3,90,000	5%	3,90,000	1.66%
Public	38,22,000	49%	82,06,213	35.10%
Total	78,00,000	100%	2,33,86,500	100%

Consequent to the rights issue, the shareholding of BSIDCL had reduced from 26% to 8.67% and the shareholding of HIL increased from 20% to 54.57%. Pursuant to the said allotment, report dated 12.05.03 under Regulation 3(4) of the Regulations for claiming exemption under Regulation 3(1) (b) of the Regulations from Regulation 11(1) was filed by HIL and the same was taken on record based on the disclosure made by the acquirer that there was no change in control over the company pursuant to the rights issue. The exemption under regulation 3(1)(b) is available to the acquirer subject to fulfillment of the condition that there will be no change in control over the Target Company.

- 1.6 Thereafter, HIL vide letter dated December 22, 2003 had made a request for an interpretive letter under the Securities and Exchange Board of India (Informal Guidance) Scheme, 2003 on the applicability of the Regulations regarding proposed amendment to the Articles of Association of the Target Company so as to enable them to acquire control over the Target

Company. Along with the said letter, Articles of the Association of the Target Company and letter of offer dated January 30, 2003 regarding rights issue made by the Target Company were forwarded to SEBI. The Article of Association was not available at the time of examining of the said report under Regulation 3(4). As per the Articles of the Association of the Target Company, it was observed that BSIDCL's right to nominate three directors (out of total 9 directors) including Chairman on the Board of the Target Company was contingent upon its holding of minimum 26% shares in the Target Company. The moment the shareholding of BSIDCL was reduced below 26%, it lost its right to nominate Chairman and Directors. Accordingly, the Acquirers were in a position to acquire control by having/continuing their own directors. Consequently, the Acquirer, prima facie, acquired the right to control the Target Company in terms of Regulation 12 of the Regulations. Since there was, prima facie, change in right to control of management, the exemption taken on record on the basis of the declaration would not have been available to them. Further, in view of the reduction in the shareholding of BSIDCL from 26% to 8.63% and consequent increase in the shareholding of the Acquirers from 25% to 56.23%, it is found that the Acquirers, prima facie, triggered the provisions of Regulation 11(1) of the Regulations.

2.0 SHOW CAUSE NOTICE

2.1 As the Acquirers had acquired further shares by way of rights issue, increasing their shareholding from 25% to 56.23% (an increase in shareholding of 31.23%) and it, later being found that they were not entitled to the exemption, as claimed by them vide their report dated 12.05.03 under Regulation 3(4), under the provisions of Regulation 3(1)(b) as there has actually been a change of control of management, the Acquirers, prima facie, violated the provisions of Regulation 11(1) and 12 of the Regulations.

2.2 The Acquirers were under an obligation to make public announcement to acquire a minimum 20% shares of the Target Company in terms of Regulation 11(1) and 12 of the Regulations within 4 days from 07.05.2003 in terms of Sub-regulation (1) and (3) of Regulation 14 of the Regulations. The Acquirers have acquired the said shares/voting rights of the Target Company without making a public announcement as required by the provisions of the Regulations. The above mentioned acquisition, without making the open offer, was prima facie found to be in violation of the provisions of Regulations 11(1) & 12 read with 14(1) and 14(3) of the Regulations. A Show Cause Notice was issued to the Acquirers on May 19, 2004 to show cause as to why action(s) under Regulation 44 and Regulation 45 of the Regulation and Sections 11, 11B, 11(4), 15H and 24 of the SEBI Act 1992, should not be taken against them for the said violations.

3.0 REPLY TO THE SHOW CAUSE NOTICE

3.1 Hindalco Industries Ltd. (HIL), one of the Acquirers, submitted their reply to the above said Show Cause Notice vide their letter dated July 01, 2004. In the said reply HIL, inter alia, submitted that:

- a. Arguing that the Show cause Notice is fallacious, HIL submitted that, BSIDCL's forfeiture of its right to appoint the Chairman and Directors on the Board of Directors of the Target Company was alleged to be a benefit or an acquisition of some additional rights to the collaborators. BSIDCL's loss was treated as the collaborators gain.
- b. By reason of BSIDCL's loss of right to appoint Chairman and 3 Directors of the Target Company, the collaborators with their enhanced shareholding from 25% to 56.23% were in a position to acquire control by having / continuing to have their own directors.
- c. Since the collaborators had acquired the right to appoint the majority of directors (by virtue of the Articles and the lapse of JV Agreement), the collaborators had acquired control over the Target Company in terms of Regulation 12.
- d. The entire show cause notice and the conclusion reached therein are based upon a complete misreading, misunderstanding, misinterpretation not only of the provisions contained in the Articles of Association of the Target Company and the JV Agreement but also of the Takeover Regulations.
- e. The JV Agreement clearly provided that so long the collaborators hold not less than 25% shares in the Target Company, "the management of the company shall vest in the Managing Director". Further, Article 138 of the Articles also provided that so long the collaborators hold 25% in the Target Company, the Managing Director of the Target Company shall be nominee of the collaborators.
- f. By reason of JV Agreement as well as Articles of Association of the Target Company, the collaborators had, even prior to the rights issue and at all material times, nominated / appointed the Managing Director and three Directors on the Board of Directors of the Target Company (including the Managing Director). i.e. to say the management of the company was already under the control of the collaborators.
- g. By reason of fall in the share holding of BSIDCL in the Target Company below 26%, it would lose its right to appoint the Chairman and the Directors would not make any difference whatsoever to the fact that the management of the Target Company was already under the control of collaborators/Acquirers.

- h. The allegation that the collaborators were not entitled to the benefit of exemption under the second proviso to the Regulation 3(1)(b) of the Regulations because there has been change in control of management is also not correct.
- i. The definition of the control under Regulation 2(1)(c) of the Regulations is not only inclusive but also exhaustive. It was further stated that majority of shareholding is just one of the methods / rights and in no circumstances; it is the decisive factor in determining the effective control. Securities Appellate Tribunal judgment in case of Swedish Match AB Vs. SEBI and Ashwin K. Doshi Vs. SEBI were quoted to this effect. Control has been exercised and continues to be exercised by the collaborators through factors other than shareholding and therefore in such circumstances, by a mere change in shareholding of the collaborators, no further control was acquired.
- j. To acquire control there has to be, 'change' of control. The definition of change as per Blacks' Law Dictionary and Oxford Dictionary was cited. According to them change means 'to make or become different', 'to transform or convert'. They asserted that the management of the Target Company already vested in the Managing Director, a nominee of the collaborator and hence the collaborators were already in control or deemed to be in control of the Target Company within the meaning of Regulation of 2(1)(c).
- k. Alternatively, and without prejudice to any other submissions, it was stated that the increase in shareholdings of the collaborators in the Target Company from 25% to 56.23% would be covered within the scope of Regulation 3(1)(e), which deals with inter se transfer of shares amongst promoters.
- >l. As per explanation ii to Regulation 2(1) (c), the acquisition of control would not be considered to be a change of control if the control acquired is equal to or less than the control exercised by the persons prior to such acquisition of control. It was stated that increase from 25% to 56.23%, the collaborators did not acquire any additional control in excess of the control exercised by them prior to the Rights Issue and hence there is no change as alleged by SEBI.
- m. The collaborators have been transparent about the whole affair, their public shareholdings, the intension to acquire additional shares, the existing legal arrangements and the expiry of JV Agreement. Further the collaborator acted in good faith and made all the necessary disclosures and filings with SEBI.

3.2.1 Pilani Investment and Industries Corporation Ltd., the other Acquirer, submitted its reply vide letter dated July 02, 2004 and stated that they have seen the copy of the letter dated July 01, 2004 addressed by HIL and have nothing further to add in addition to what had been stated by HIL.

3.2.2 In so far as Gwalior Rayon Silk Mfg. (Wvg.) Co. Ltd. which is one of the noticees, in view of their reply that their entire shareholding was sold much prior to the Rights Issue and that they are not a PAC with the acquirer on the relevant date, no directions are necessary and their explanation is accepted.

4.0 PERSONAL HEARING AND REPLY

4.1 In the interest of natural justice, an opportunity of personal hearing was granted to the Acquirers on October 14, 2004. The hearing took place as scheduled on October 14, 2004 which was attended by Ms. Zia Mody, Mr. Shobhan Takore and Mr. Aashit Shah of AZB Partners, Mr. K K Maheshwari and Mr. M R Prassana of Aditya Birla group and Mr Kashliwal of Hindalco. They reiterated the submissions made by Acquirers in the written submissions contained in their letter dated July 01, 2004. Pursuant to the hearing, the parties were also given 10 days time to file the written submissions. On October 25, 2004, the Acquirers submitted the written submissions reiterating their earlier stand and further submitted, inter alia, as follows :

- a. They already controlled the management of the Target Company prior to the rights issue by virtue of the Managing Director being their nominee and the management right vested in such Managing Director.
- b. Pursuant to the rights issue, there was no change of control of management as they continued to have the right to appoint the Managing Director and, therefore, the collaborators were rightfully entitled to the exemption under Regulation 3(1)(b) of the Takeover Regulations.
- c. Since the acquisition of an additional 31.23% of the shares of the Target Company pursuant to the rights issue was within the exemption under Regulation 3(1)(b) as shown above, the provisions of Regulation 11(1) as alleged in paragraph 10 of the show cause notice are not attracted.
- d. Since the acquisition of an additional 31.23% of the shares of the Target Company pursuant to the rights issue was within the exemption under Regulation 3(1)(b) as shown above, the provisions of Regulation 12 as alleged in paragraph 11 of the show cause notice are not attracted.
- e. The collaborators were not under any obligation to make an announcement to acquire a minimum of 20% shares of the Target Company within 4 working days of May 7, 2003, as alleged in paragraph 13 of the show cause notice and,

- f. The collaborators should be absolved of all the charges as alleged by SEBI in relation to Regulations 11(1), 12, 14(1) and 14(3) of the Takeover Regulations and,
- g. No action should be taken by SEBI against the collaborators pursuant to Regulations 44 and 45 of the Takeover Regulations and Sections 11, 11B, 11(4), 15(H) and 24 of the SEBI Act, 1992 and the show cause notice should be withdrawn.

5.0 ISSUES

- 5.1 I have taken into consideration the facts and circumstances of the case, both oral and written submissions made by the Acquirers and also the documents submitted by them in support of their submissions.
- 5.2 The issues, which arise for consideration are:
 - a. Whether the Acquirers acquired the control in terms of Regulation 2(1)(c) pursuant to the acquisition of 31.23% of the equity shares on May 07, 2003 when allotment of the same was made pursuant to the rights issue attracting the provisions of Regulation 11(1) and 12.
 - b. If yes, when did the obligation on the part of the Acquirers to make the public announcement arise?

6.0 CONSIDERATION OF THE ISSUES

- 6.1 At the outset, it will be pertinent to refer to the relevant provisions of

Regulation 11(1), 12, 14(1) and 14(3) of the regulations in force at the relevant time .i.e. 07.05.2003 which are reproduced hereunder:

Regulation 11(1)- (Consolidation of Holdings)

"No acquirer, who together with persons acting in concert with him has acquired, in accordance with the provisions of law, 15% or more but less than 75% of the shares or voting rights in a company, shall acquire either by himself or through persons acting in concert with him any additional shares or voting rights entitling him to exercise more than 5% of the voting rights in any financial year ending March 31, unless such acquirer makes a public announcement to acquire shares in accordance with the Regulations."

Regulation 12- Acquisition of Control over a Company

"Irrespective of whether or not there has been any acquisition of shares or voting rights in a company, no acquirer shall acquire control over the Target Company, unless such person makes a public announcement to acquire shares and acquires such shares in accordance with the Regulations."

Regulation 14(1) and 14(3) - deals with Timing of the public Announcement of offer, which reads as under:

Regulation 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".

Regulation 14(3) : "The public announcement referred to in Regulation 12 shall be made by the merchant banker not later than four working days after any such change or changes are decided to be made as would result in the acquisition of control over the Target Company by the acquirer".

- 6.2 **Consideration of the first issue:** Whether the Acquirers acquired 'control' in terms of Regulation 2(1)(c) pursuant to the acquisition of 31.23% of the equity shares on May 07, 2003 when allotment of the same was made pursuant to the rights issue attracting the provisions of Regulation 11(1) and 12 ?

- 6.2.1 Reg. 11(1) deals with acquisition of **additional shares or voting rights entitling him to exercise more than 5% of the voting rights**. In the instant case, I find that in February 2003, the Target Company offered further equity shares in the Company by way of a right issue to the existing shareholders. The offer was contained in the Letter of Offer dated January 30, 2003. The Board of Directors of the Target Company while authorizing the rights issue by the resolution dated March 20, 2002 provided that the promoter shareholders should confirm to the company at least ten days before the closure of the rights issue whether they will subscribe their share of the rights issue or other promoter/third party shall subscribe to their share of rights shares. BSIDCL decided that it did not want to subscribe to the rights issue. In accordance with the said decision by BSIDCL, it was disclosed in the Letter of Offer that BSIDCL, by its letter of July 1, 2002 informed the company that the Government of Bihar had intimated to BSIDCL that it "will not be proper to invest further" by the Government of Bihar/BSIDCL in the Company. HIL by its letter dated June 18, 2002 undertook that it will subscribe to its rights entitlement in full, and in addition that it intended to apply for additional shares to the extent the issue was undersubscribed. It was

further stated that such acquisition of shares, if allotted to HIL would be in accordance with the provisions of Regulation 3(1) (b) of the Regulations and will therefore be exempt from the applicability of Regulations 11 and 12 of the Regulations. It was also stated in the letter of offer and the post-allotment fillings made with the Securities and Exchange Board of India that there was no change of control by virtue of the subscription by HIL to the additional shares in the rights issue.

6.2.2 Further, On May 7, 2003, shares were allotted pursuant to the rights issue.

The shareholding of the company before and after the rights issue is as follows :

Shareholder	Pre-Rights Issue		Post Rights Issue	
	No. of Shares	Percentage	No. of Shares	Percentage
BSIDCL	20,28,000	26%	20,28,000	8.67%
Hindalco	15,60,000	20%	1,27,62,287	54.57%
Pilani	3,90,000	5%	3,90,000	1.66%
Public	38,22,000	49%	82,06,213	35.10%
Total	78,00,000	100%	2,33,86,500	100%

From the foregoing, it is noted that the cumulative shareholding of the Acquirers rose from 25% to 56.23% i.e. an increase in shareholding of 31.23% shares. Pursuant to the rights issue, HIL filed an exemption application under regulation 3(4) of the Regulations for claiming exemption from Regulation 11(1) under Reg. 3(1) (b) of the Regulations. The exemption application was examined and based on the submissions i.e. that there is no change in control of the Target Company it was taken on record.

6.2.3 HIL vide letter dated December 22, 2003 had made a request for an interpretive letter under the Securities and Exchange Board of India (Informal Guidance) Scheme, 2003 on the applicability of the Regulations regarding proposed amendment to the Articles of Association of the Target Company so as to enable them to acquire control over the Target Company. At para 11 of the letter cited, it was stated as under :

" Consequently, with the current shareholding of 56.23% in the company, the collaborators would be in a position to control the election of the majority of the Board of Directors which may result in change in control of the management of the company" Along with the said letter, Articles of the Association of the Target Company and letter of offer dated January 30, 2003 regarding rights issue made by the company were forwarded to SEBI. It may be noted that these documents were not made available at the time of examining of the said report u/r 3(4).

6.2.4 On perusal of the Articles of Association, I find that the salient provisions contained in Articles 101, 124 and 138 of the Articles of Association of the Target Company provide as under -

(a) **Article 101-** During such time BSIDCL shall hold 26% shares in the Target Company it shall have the right to appoint initially not more than 3 directors on the Board of the Target Company.

(b) **Article 101-** During such time collaborators / Acquirers shall hold 25% shares in the Target Company it shall have the right to appoint initially not more than 3 directors on the Board of the Target Company.

(c) **Article 124-** During such time as BSIDCL shall hold not less than 26% in the Target Company it shall have right to nominate the Chairman of the Board of Directors.

(d) **Article 138-** So long as the collaborators hold 25% in the Target Company the Managing Director of the Target Company shall be nominee of the collaborators.

The JV Agreement provided that so long as the collaborators hold not less than 25% in the Target Company, the management of the company shall vest in the Managing Director.

On going through the above stated stipulations in the Articles, I find that the right of BSIDCL to nominate the Chairman and the three directors on the Board of the Target Company is dependent upon its holding of minimum 26% shares in the Target Company. The moment the shareholding of BSIDCL is reduced below 26% it has lost its right to nominate Chairman and 3 other directors. The contention of the Acquirer that the whole show cause notice proceeds on fallacious and untenable allegations that BSIDCL's loss was the collaborators' gain is not correct. The loss in the voting rights of BSIDCL consequent to its refusal to subscribe to the Rights Issue and the acquisition of additional shares by the acquirers pursuant to the refusal of BSIDCL to subscribe to the Rights Issue had resulted in increase of its shareholding as seen above. Further, the loss of right to nominate the three directors (out of total 9 directors) including the Chairman, which was dependent upon BSIDCL's holding a minimum of 26% shares of the Target Company, is the corresponding gain of the acquirers. Consequent to the reduction in the shareholding of BSIDCL from 26% to 8.67%, it has lost the right to appoint the requisite number of Directors and more importantly the Chairman who has the casting vote. Consequently, Articles 101 and 124 of the Articles of Association, that permit BSIDCL to nominate three Directors one of whom is to be the Chairman, will require to be amended. It is also significant to know that earlier with a 26% shareholding BSIDCL was in a position to block a special resolution in terms of Section 189 of the company's act, 1956 which requires passing of the special resolution by a majority

of not less than ¼th of the members entitled to vote. With the reduction of BSIDCL's shareholding from 26% to 8.67% and consequent reduction of voting rights, it will no longer be in position to block a special resolution.

- 6.2.5 I further note that the report of HIL filed with SEBI on 12.05.2003 under Regulation 3(4) for claiming exemption under the provisions of Regulation 3(1)(b) of the Regulations stating " there is no change in control of the management of the company and there is no change in the Board of Directors and the promoters will remain the same " is not correct. As already mentioned, consequent to BSIDCL's decline in shareholding from 26% to 8.67%, it has lost its right to appoint the requisite number of the Directors and the Chairman as contemplated by the Article 101 and 124. Thus there is change in right to control of management of the Target Company pursuant to the increase in the shareholding of the Acquirers from 25% to 56.23% and BSIDCL's fall in shareholding from 26% to 8.67%.
- 6.2.6 I further find the argument put forth by the Acquirer that the collaborators already controlled the management of the Target Company prior to the rights issue by virtue of the Managing Director being their nominee and the management vesting in such Managing Director (by virtue of Clause 14, page 7 of the J V Agreement and Article 138 of the Articles of Association) is not tenable. Here it is pertinent to note that from the cumulative reading of the "Powers of the Board" in the Articles of Association (Article 130 – 137), it becomes clear that the control of the company shall vest in the Board of the Directors. Further, I note from the cumulative reading of the said Articles that it is from the point of view of administrative convenience and for day to day affairs, the general power of superintendence is vested with the Managing Director. Further, attention is drawn to Article 122 and 123 of the Articles of Association where it is specifically stated that any question arising at any meeting of the Board shall be decided by the majority of the votes, and in case of equality of votes, the Chairman shall have second or casting vote. Hence, argument of the Acquirer that they already controlled the management of the Target Company and that there is no change in control subsequent to the Rights Issue is not tenable.
- 6.2.7 From Article 138, I note that Managing Director of the Target Company shall be normally of the collaborator / Acquirer and he will be appointed in consultation with BSIDCL, so long the collaborators and their nominees hold 25% of the equity share capital of the company. The Articles and the JV Agreement required BSIDCL to hold minimum of 26% shares of the Target Company in order to appoint the requisite number of Directors including the Chairman or to be consulted in the appointment of the Managing Director. After the acquisition of the shares pursuant to the rights issue, the shareholding of the Acquirers increased from 25% to 56.23% and those of BSIDCL got reduced from 26% to 8.67% and hence BSIDCL lost the right to appoint the three directors, including the Chairman and in a way lost the relevance to be consulted by the collaborator while appointing the Managing Director. From the foregoing, I find it not tenable that at all material times, the collaborators nominated / appointed the Managing Director and three Directors of the Board (including the Managing Director) and BSIDCL had no say in it.
- 6.2.8 From the Schedule to consolidated financial statement given in Annual Report for the Year 2002 - 2003 of HIL, I find from notes to the account (point 17) that the Target Company (BCCL) has allotted 80,82,287 equity shares to HIL and its subsidiary on 7th May, 2003 and consequently BCCL has become subsidiary of HIL. I note that Section 4 of the Companies Act deals with as to when a company becomes the subsidiary of the other. Here, it becomes pertinent to reproduce the relevant portion of the said section.

Section 4:

Meaning of "holding company" and "subsidiary". —(1) For the purposes of this Act, a company shall, subject to the provisions of sub-section (3), be deemed to be a subsidiary of another if, but only if, —

(a) that other controls the composition of its Board of directors; or

(b) that other —

(i) where the first-mentioned company is an existing company in respect of which the holders of preference shares issued before the commencement of this Act have the same voting rights in all respects as the holders of equity shares, exercises or controls more than half of the total voting power of such company;

(ii) where the first-mentioned company is any other company, holds more than half in nominal value of its equity share capital; or]

(iii)

(2)

From the foregoing it is clear that pursuant to the issue of 80,82,287 equity shares of the Target Company to HIL and its subsidiary, the Target Company became the subsidiary of HIL. Consequently HIL acquired the right to control the composition of the Board of Directors of the Target Company. Further Sub section 2 clearly states the situations wherein a company will be in a position to control the composition of the Board of directors of the other company.

Sub section 2 states that,

For the purposes of sub-section (1), the composition of a company's Board of directors shall be deemed to be controlled by another company if, but only if, that other company by the exercise of some power exercisable by it at its discretion without the consent or concurrence of any other person, can appoint or remove the holders of all or a majority of the directorships; but for the purposes of this provision that other company shall be deemed to have power to appoint to a directorship with respect to which any of the following conditions is satisfied, that is to say: —

(a) that a person cannot be appointed thereto without the exercise in his favour by that other company of such a power as aforesaid;

(b) that a person's appointment thereto follows necessarily from his appointment as director or manager of, or to any other office or employment in, that other company; or

(c) that the directorship is held by an individual nominated by that other company or a subsidiary thereof.

Since the Target Company had already become the subsidiary of HIL, I note that HIL had acquired the right to control the composition of the Board of directors of the Target Company. BSIDCL had lost its right to appoint the requisite number of the directors including the Chairman and the right to be consulted in case of the appointment of the Managing Director. It is further noticed that Schedule 21, Notes on Accounts – Consolidated Financial Statements of for the financial year 2002 – 2003 states as under :-

“BCCL has allotted 80, 82, 287 equity shares to the company and its subsidiary on 07.05.2003. consequently BCCL has become subsidiary of the company.” (underling supplied)

6.2.9 Further from the list of the Board of directors of the Target Company as submitted to the Registrar of the Companies, Bihar in Form No. 32, I observe that till March 2003 and pre rights issue, BSIDCL was having three directors including the Chairman on the Board of directors of the Target Company. However, after the rights issue, Shri Ashok Kumar, Chairman, unilaterally withdrew from the Chairmanship of Target Company since 19.04.04 and another director, Shri V.N. Sharma (a representative of BSIDCL), who was appointed on 24.05.03 ceased to hold the post after the expiry of one year from the date of the appointment. From the list of the Board of directors as on 20.01.05, I find that Shri Vijoy Prakash who was appointed as director on 23.04.04 continue to be the sole representative of BSIDCL on the Board of Directors of the Target Company. In such a situation, wherein BSIDCL has only one representative and HIL has three other directors including the Managing Director, the right to control the management will certainly rest with them. This was not the case before the rights issue. Only after the rights issue of the Target Company on May 07, 2003 to HIL and its subsidiary, the Target Company became the subsidiary of HIL and BSIDCL lost the right to appoint the three directors, including the Chairman on the Board of directors of the Target Company.

6.2.10 As to the alternative argument put forth by the Acquirer that the increase in shareholdings of the collaborator in the Target Company from 25% to 56.23% would be covered within the scope of Regulation 3(1) (e), which deals with inter se transfer of shares amongst promoters, I find that, in this case, there is no inter se transfer of shares. It is a case of acquisition of additional shares by way of rights issue to the existing shareholders. There was no transfer of existing shares among the promoters fulfilling the requirement of the regulations. Hence, the argument put forth by the Acquirer is untenable.

6.2.11 Dealing with the contention that as per explanation ii to Regulation 2(1) (c), the acquisition of control would not be considered to be a change in control if the control acquired is equal to or less than the control exercised by the persons prior to such acquisition of control, I note that the submission that the Acquirers did not acquire any additional control in excess of the control exercised by them prior to the rights issue valid. As already clearly brought out, due to BSIDCL's fall in shareholding from 26% to 8.67%, it has lost the right to appoint the requisite number of directors, including the Chairman. The Chairman had a second or casting vote, in case of equality of the votes. Such an authority / casting vote is not a mere formality and has considerable importance, in pending decisions having major strategic or financial implications. BSIDCL's loss of such a power and obviously, its renunciation resulted in collaborators/Acquirers, gaining the right to exercise control over the Target Company. BSIDCL can no longer block a special resolution So, the contention that the Acquirer did not acquire any additional control in excess of the control exercised by them prior to the rights issue and hence there was no change in control is not correct.

6.2.12 Further, I note that once the right to control / voting right is acquired; it is enough to attract the provisions of the Regulations. It is of no consequence, whether such control / voting rights have in fact been exercised or not.

6.2.13 In view of the above, I find that there has been an increase in shareholding of the Acquirers from 25% to 56.23% (an increase of 31.23%) which is much beyond the creeping acquisition limit of 5% as contemplated by Regulation 11(1) and consequently there has been change in right to control the management in the Target Company attracting the provisions of Regulation 12 of the Regulations.

6.3 Consideration of Second Issue : If yes, when did the obligation on part of the Acquires to make public announcement arise?

6.3.1 Further, in terms of regulation 11(1), if an Acquirer who is holding 15% or more shares, acquires additional shares entitling him to exercise more than 5% of the voting rights in any financial year ending March 31, then the Acquirer is required to make an open offer to the shareholders of the Target Company in accordance with the Regulations. In the instant case, the Acquirers were already holding 25% shares prior to the acquisition of 31.23% equity share. On May 07, 2003 the Acquirers acquired additional 31.23% shares / voting rights of the Target Company without making the public announcement in accordance with the Regulations. Though the Acquirers had got the exemption from the applicability of Regulation 11(1) under the provisions of Regulation 3(1) (b) of the Regulations, the said exemption was granted on the basis of the declaration by the Acquirer that the acquisition of the securities did not result in the change of control of management. Subsequently, on December 22, 2003 when HIL had made a request for an interpretive letter under the SEBI (Informal Guidance) Scheme, 2003 on the applicability of the Regulations regarding the proposed amendment to the Articles of the Target Company, on going through the Articles (which was not furnished earlier), it was found out that there has already been a change in control over the Target Company for the reasons already mentioned hereinabove.

6.3.2 From the above, it becomes evident that the relevant date for making public announcement would be the date of acquisition of the additional equity shares pursuant to the rights issue on May 07, 2003.

6.3.3 In view of the above, the Regulation 11(1) was triggered on the date of acquisition of the additional 31.23% equity shares pursuant to the rights issue carrying voting rights i.e. on May 07, 2003 and therefore the obligation on the part of Acquirers to make the public announcement arose on the same date, i.e. on May 07, 2003 which was required to be made within 4 working days from the said date.

7.0 CONCLUSION

7.1 In view of the aforesaid, the acquisition of 31.23% equity shares / voting rights of the Target Company by the Acquirers on May 07, 2003 pursuant to the rights issue, was not eligible for exemption under Regulation 3(1) (b) as contended by the Acquires as there has been a change of right to control the management as a result of the acquisition of the securities issued by way of rights issue by the Target Company and the same is hit by the provisions of Regulation 11 and 12 of the Regulations.

7.2 I find that the Acquirers have violated Regulation 11(1) and Regulation 12 read with sub-regulation (1) & (3) of Regulation 14, as the Acquirers have acquired 31.23% shares / voting rights in the Target Company without making public announcement to acquire shares / voting rights of the Target Company in accordance with the said Regulations.

8.0 ORDER

8.1 In view of the findings made above and in exercise of the powers conferred under sub-section (3) of Section 4 of SEBI Act, 1992 read with Regulations 44 (f) of the Regulations, I hereby direct the Acquirers, viz., Hindalco Industries Ltd. and Pilani Investments Corporation Ltd. to make public announcement as required under Chapter III of the Regulations taking June 18, 2002 i.e. the date on which HIL has expressed its willingness to the target company to subscribe to the unsubscribed portion in the rights issue, as the reference date for calculation of offer price. Once a decision is taken which results in acquisition of shares / voting rights or control, then public announcement must precede such acquisition or control. That is the decision that will later on result in acquisition or taking control. This view on the reference date is supported by the judgment of Division Bench of Hon'ble High Court in B P Plc Vs. SEBI (2001) 24 SCL 469 (Bom). The public announcement shall be made within 45 days of passing of this order.

8.2 Further, in terms of sub regulation (12) of regulation 22, the payment of consideration to the shareholders of the Target Company has to be paid within 30 days of the closure of the offer. The maximum time period provided in the said Regulations for completing the offer formalities in respect of an open offer, is 120 days from the date of public announcement. The public announcement in the instant case ought to have been made by June 22, 2002 taking June 18, 2002 as the relevant date. Accordingly, the shareholders were entitled to receive the payment of consideration by October 20, 2002. Since no public announcement for acquisition of shares of the Target Company has been made, which has adversely affected the interest of shareholders of Target Company, it would be just and equitable to direct the Acquirers to pay interest @ 10% per annum on the offer price. Therefore, the Acquirers are hereby directed to pay interest @ 10% per annum to the shareholders in terms of Regulation 44 (i) of the said Regulations for the loss of interest caused to them from

October 21, 2002 till the date of actual payment of consideration for the shares to be tendered / accepted in the offer directed to be made by the Acquirers.

Place : Mumbai
Date : February 18, 2005

G. N. BAJPAI
CHAIRMAN
SECURITIES AND EXCHANGE BOARD OF INDIA