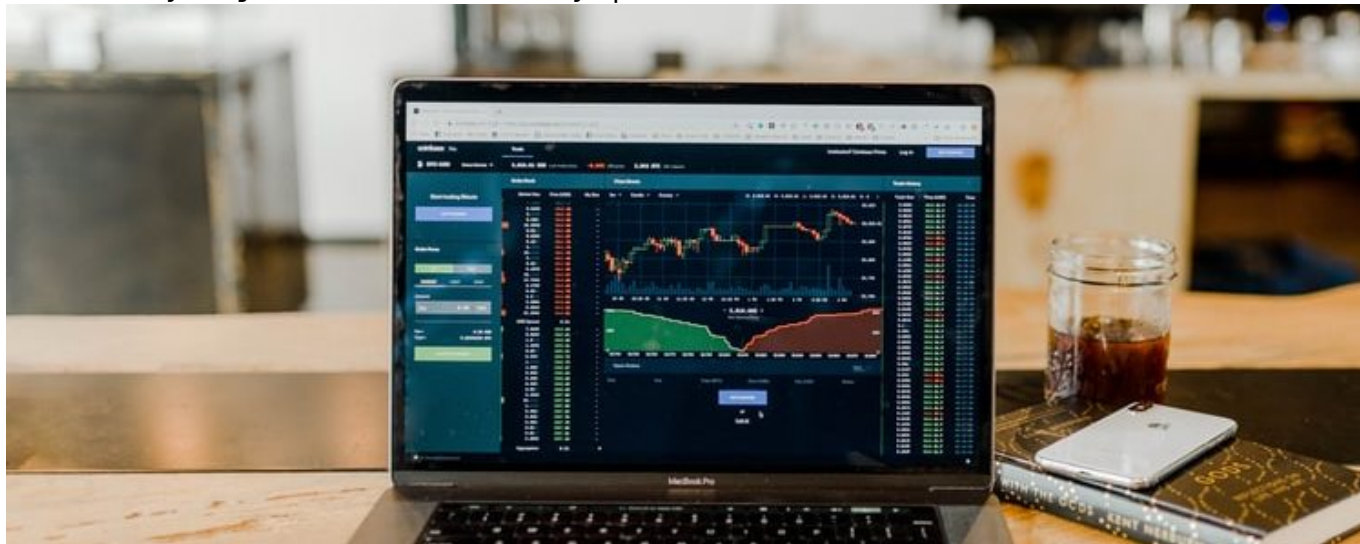


Minority Shareholders – “Squeezed Out?”

written by Rajashree Devchoudhury | March 24, 2020



Minority Shareholders Scheme of Arrangement

The Ministry of Corporate Affairs (“MCA”) vide its recent set of notifications dated February 3, 2020, has brought in a new regime for taking over minority shareholders through a scheme of arrangement to be placed before and approved by the National Company Law Tribunal (“NCLT”)[1].

Recent amendments

The much-anticipated sub-sections 11 and 12 of Section 230 of the Companies Act, 2013 (the “Act”) have eventually been notified by the MCA, effective from February 03, 2020. In addition to that, MCA has also inserted a new sub-rule 5 in Rule 3[2]

of the Companies (Compromises, Arrangements and Amalgamation) Rules, 2016 (the “Rules”), and Rule 80A[3]

in the National Company Law Tribunal Rules, 2016 (the “NCLT Rules”) in order to set forth the procedural aspects of the takeover rules especially pertaining to minority shares. The MCA, vide these amendments, has for the first time attempted to encompass private and unlisted companies under the takeover

regime, which was until now associated with listed companies under the takeover

regulations of the Securities and Exchange Board of India (“SEBI”).

Background

The newly notified provisions have been incorporated in the Act and the Rules with an object of facilitating the acquisition of minority shareholders by the majority shareholders in a company. Prior to the notification, the squeezing out of minority shareholders was regulated under Section 236 of the Act. It was necessary to procure the consent of a minimum of 90% of the shareholders of a company in order to ensure the acquisition of the minority shares. This, however, has led to a situation whereby the majority

shareholders of a company would find the acquisition of minority shareholders to be virtually impossible on account of lack of strength of majority shareholders and the same would result in long-drawn legal battles between the shareholders.

Now with the introduction of sub-sections 11 and 12 of Section 230 in

the Act together with the insertion of the new sub-rule 5 in Rule 3 of the Rules, shareholders holding only 75% of the shares in the company may formulate a scheme and obtain approval from the NCLT to acquire the shares of the minority

members of the company subject to payment of a fair price.

Overview of the new regime

Under the new regime,

shareholders holding minimum 75% of the equity shares carrying voting rights, including depository

receipts entitling its holders voting rights, shall present

a scheme of arrangement containing a 'takeover offer' along with an application before the NCLT.

It is pertinent to note that the expression 'takeover offer' has not been defined under the Act, however, from a plain reading of the amendments, it may

be construed that the term 'takeover offer' in this context would simply mean a

scheme towards the acquisition of the shares of the minority shareholders.

The new takeover

regime makes it mandatory to procure a report regarding the fair value/price of

the shares of the company through a registered valuer. The said report shall be

prepared after taking into consideration the highest price paid by any person or group of persons for the acquisition of shares of the concerned company during

the last 12 months. Further, the registered valuer, while determining a fair price of the shares, shall take into consideration valuation parameters such as

return on net worth, book values of shares, earnings per share, price earning multiple

vis à vis the industry average and such other customary parameters for valuation of shares of such companies.

Significant

Changes

One of the significant changes brought in by the

new takeover regime is the obligation on part of the members acquiring the shares of the minority to deposit a minimum 50% of the total takeover offer in

a separate bank account designated only for the takeover offer. Also, the details of such account shall be required to be included in the application to

be filed before the NCLT.

Moreover, in the

second explanation to the sub-rule 5 of Rule 3 of the Rules, it is stated that any

transfer or transmission of shares vide a contract or succession or any transfer made in pursuance of any statutory/regulatory requirement shall not be

a subject matter of this new takeover regime.

Furthermore,

the new regime provides for a grievance redressal mechanism. Under the newly notified Section 230(12), any shareholder of an unlisted company, aggrieved by

a takeover offer, may approach the NCLT by making an application as stipulated

in the new rule 80A of the NCLT Rules.

Analysis

Having a cursory reading of the new amendments, it may be observed that shareholders with 75% voting rights may squeeze out minority shareholders. However, it is pertinent to take into account that the new regime

also protects the minority shareholders by providing them an opportunity to approach the NCLT with their grievances about the takeover offer. Further, in an attempt to protect the interests of the minority shareholders, the new amendments make it compulsory to deposit a minimum of 50% of the takeover offer

in a separate bank account.

The computation of the

threshold of minority/majority shareholders through equity shares and other securities carrying voting rights may lead to uncertainties and all the members

may not be truly represented in matters involving takeover offer of minority shareholders. By restricting the class of shareholders, the amendment may lead

to various interpretations of majority/minority on account of various types of

instruments being available for acquiring interests or making investments in companies

as in vogue.

Conclusion

It will be interesting to observe whether the new amendments will protract the takeover process or make it efficient and time-saving. Thus, the coming days and the attitude of the courts will only determine the effectiveness of the new amendments to the Act and the Rules.

Contributed By - Rajashree Devchoudhury

Designation - Senior Associate

King Stubb & Kasiva,

Advocates & Attorneys

[Click Here to Get in Touch](#)

[New Delhi](#) | [Mumbai](#) | [Bangalore](#) | [Chennai](#) | [Hyderabad](#) | Kochi

Tel: [+91 11 41032969](tel:+911141032969) | Email: info@ksandk.com