

Evolution of the Definition of 'Control' Under Indian Law and Regulations



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Under Indian law, corporate control is a relevant consideration to determine the applicability of various restrictions and compliance requirements, including those under foreign investment law, insurance law, insolvency law as well as those under company and securities law.

The concept of 'control' was first defined by the Securities Exchange Board of India ("SEBI") under the order to outline when a mandatory bid requirement would be triggered under its takeover Regulations. The definition adopted by SEBI has subsequently formed the basis for the evolution of definitions in other legislations, which have largely adopted the approach of the SEBI, with suitable modifications.¹ Accordingly, this article seeks to examine the evolution and scope of this definition under the takeover Regulations.

Adopting subjective tests for control

Since 1997, SEBI has defined the concept of control qualitatively. In the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997, control was defined to "include the right to appoint majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders agreements or voting agreements or in any other manner." This definition continued under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, ("**Takeover Regulations**") following the recommendations of the Takeover Regulations Advisory Committee in its Report of 2010.

The rationale for adopting a qualitative approach to evaluating control is to prevent an abuse of process, and to enable a fact-based evaluation of the control exercised by parties. This approach allows for a fact based analysis of 'de facto' control in each case, including where control is acquired through affirmative rights.² While this approach may assist minority shareholders where investors are seeking to circumvent mandatory bid requirements, it creates a large amount of uncertainty that could prevent new investment. This could both prove to be adverse to

developing a market for corporate control and to value maximisation for minority shareholders in some cases.

Uncertainty in applying the test for control

This uncertainty is also exacerbated by the manner in which this provision for control has been interpreted. For instance, in *Subhkam Ventures*³ while assessing whether certain affirmative voting covenants, requiring the affirmative vote conferred control on an investor, the Securities Appellate Tribunal ("SAT") held that these investors would not be considered to have conferred control over the investor since the affirmative voting rights were not on matters "in the nature of day to day operational control over the business of the target company. So also, they are not in the nature of control over either the management or policy decisions of the target company."⁴ More specifically, the Securities Appellate Tribunal held that the control "is a proactive and not a reactive power... It is a positive power and not a negative power... The test really is whether the acquirer is in the driving seat. To extend the metaphor further, the question would be whether he controls the steering, accelerator, the gears and the brakes... In other words, the question to be asked in each case would be whether the acquirer is the driving force behind the company and whether he is the one providing motion to the organisation. If yes, he is in control but not otherwise. In short control means effective control."⁵

However, this matter remained open following its appeal to the Supreme Court, as the Supreme Court dismissed it as settled while "keeping the question of law open" clarifying "that the impugned order passed by the SAT will not be treated as a precedent."⁶

The uncertainty had since continued, with SEBI taking different positions in different cases. For instance, in the case of *Kamat Hotels*,⁷ SEBI applied the same test that was applied in *Subhkam* by the Securities Appellate Tribunal. However, in other cases, the SEBI has applied a different understanding of the concept of 'control'. For instance, in the case of *NDTV*,⁸ SEBI has held that the existence of a call option as well as certain veto rights, together amounted to acquisition of control. Critically, this was held without the call option in fact being exercised, and despite contentions that the factual control and management stayed with the original promoters.

Brightlines for Control?

On account of the ambiguity such differing interpretations create, there have been calls to reform the test for control under the Takeover Regulations. In 2017, SEBI released a Discussion Paper on Brightline Tests for Acquisition of 'Control' under SEBI Takeover Regulations. In this

paper, SEBI sought comments on proposals to modify the test for control. It proposed either adopting a 'numerical test' to define control or by explicitly clarifying that certain rights are protective in nature and do not amount to exercise of control.⁹ However, since then, no amendment has been made to the Takeover Regulations to incorporate either of the two proposals.

While legislative changes to SEBI's Takeover Regulations have not fructified to provide more certainty to the concept of control, there has been some judicial development on the concept of control in other laws.

Most significantly, the concept of control was discussed in context of insolvency law by the Supreme Court of India in *ArcelorMittal India v. Satish Kumar Gupta*.¹⁰ In this case, the Court examined who would be a person in "management and control" of a corporate debtor, who should be barred from proposing a resolution plan under section 29A of the Insolvency and Bankruptcy Code, 2016 ("Code"). Since the term control is not defined in the Code, the definition of control in the Companies Act, 2013 (which is substantially similar to the definition under the Takeover Regulations) formed the basis for interpretation. Here, the Supreme Court quoted the SAT judgement in *Subhkam Ventures* with approval, and held that to be barred under section 29A, a person would have to have "*de facto control of actual management or policy decisions that can be or are in fact taken.*" Crucially, a basis for this was that the term control in section 29A is preceded by the term management, and consequently, "*in the expression "management or control", the two words take colour from each other, in which case the principle of noscitur a sociis must also be held to apply.*

Thus viewed, what is referred to in sub-clauses (c) and (g) is de jure or de facto proactive or positive control, and not mere negative control which may flow from an expansive reading of the definition of the word "control" contained in Section 2(27) of the 79 Companies Act, 2013, which is inclusive and not exhaustive in nature." While this still leaves ambiguity on the exact application of the definition of control in other circumstances, perhaps this could serve as a step forward in crystallising the concept of control in other laws.

In another case of *Chintalapati Srinivasa Raju v. Securities and Exchange Board of India*,¹¹ the Supreme Court, while assessing whether an executive director could be considered a promoter on account of being person in control under SEBI Insider Trading Regulations, specifically held that "*it is the judicial duty to take note of the immediate and proximate facts and circumstances surrounding the events on which the charges/allegations are founded and to reach what would appear to the Court to be a reasonable conclusion therefrom.*" This ruling too provides comfort that judicial determination on control will take into account the surrounding facts of cases. Even as the definition of control has evolved in Indian law, there has been continuing uncertainty on how it will apply in practice. While recent developments appear to signal some will to provide clarity and certainty to the interpretation of control, there is significant scope to provide more certainty on the concept of control both in the SEBI Takeover Regulations and across other laws. This certainty will go a long way towards improving the Ease of Doing Business in India.

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¹ See: Umakanth Varottil, "Control" Untouched in the Takeover Regulations: A Case of Regulatory Inertia (IndiaCorpLaw Blog, 9 September 2017) available at <https://indiacorplaw.in/2017/09/control-untouched-takeover-regulations-case-regulatory-inertia.html>

² SEBI, Report of the Takeover Regulations Advisory Committee (2010), paras 3.2 to 3.7 available at https://www.sebi.gov.in/sebi_data/attachdocs/1287826537018.pdf

³ Appeal No. 8 of 2009 before the Securities Appellate Tribunal, decision dated 15.01.2010

⁴ Id. at Para 8

⁵ Ibid. note 3 at Para 6

⁶ Civil Appeal No. 3371 of 2010, order dated 16 November 2011 available at <https://main.sci.gov.in/jonew/bosir/orderpdf/1406710.pdf>

⁷ In the matter of Kamat Hotels (India) Limited, WTM/GM/EFD/DRAIII/20/MAR/2017 (SEBI), order dated 31 March 2017 available at https://www.sebi.gov.in/sebi_data/attachdocs/1491380833690.pdf

⁸ In the matter of NDTV Ltd. in respect of Vishvapradhan Commercial Private Ltd., WTM/GM/EFD/ 31 / 2018-19 (SEBI), order dated 26 June 2018 available at https://www.sebi.gov.in/enforcement/orders/jun-2018/order-against-vishvapradhan-commercial-private-ltd-vcpl-in-the-matter-of-ndtv_39359.html

⁹ SEBI, SEBI Discussion Paper on Brightline Tests for Acquisition of 'Control' under SEBI Takeover Regulations (2016) available at https://www.sebi.gov.in/sebi_data/attachdocs/1457945258522.pdf

¹⁰ (2019) 2 SCC 1, Paras 48-50

¹¹ (2018) 7 SCC 443, Para 20, citing SEBI v. Kishore R. Ajmera, (2016) 6 SCC 368