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Minority Squeeze Out:

A strong new provision under section 236 of the Companies Act, 2013

Pammy Jaiswal

pammy@vinodkothari.com

Rahul Maharshi

rahul@vinodkothari.com

Corporate Law Services Division

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Background

Although the concept of squeezing out the minority shareholders has always been practically present in the corporate sector around the globe, there was absence of a backing statute under the Companies Act, 1956 ('Erstwhile Act'). However, such concept has been explicitly introduced under the provisions of the Companies Act, 2013 ('Act') which has been enforced vide Ministry of Corporate Affairs notification dated 7th December, 2016¹. The skeptic situation of the dominance of majority rule and at the same time protecting the rights and interest of the minority has always been the area of controversy and discord. It is imperative for the statute to ensure that the powers of the majority are within reasonable bounds, hence not resulting in oppression of the minority. But the practical implication of protecting minority interests while taking strategic business decisions often create obstacles which lead to prolonged legal battle.

Prevalent practices for squeezing out of the minority shareholding from entity company around the globe has generally been:

1. Takeovers;
2. Arrangements;
3. Mergers;
4. Conversion of securities to Equity; and
5. Capital Reduction.

"Squeeze out" in context of acquisition and takeover means a situation where the minority shareholders are squeezed or dragged out of their shareholding in the transferor company by the majority shareholders by purchasing their stake inspite of disagreement by the former.

'Minority shareholding' has not been specifically defined under the Act, however, section 236 of the Act uses the word Minority shareholding in respect of registered holders of the issued equity shares of the company not exceeding ten percent.

This write-up endeavors to conceptualize and analyze the provisions of acquiring the stake of minority equity shareholders besides comparing the international scenario on the same.

Squeezing out minority equity shareholders- The Indian perspective

Section 236 of the Act provides for the purchase of minority shareholding by the majority shareholders in accordance with the provisions of the section read with the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016² ('CAA Rules, 2016').

¹http://www.mca.gov.in/Ministry/pdf/commencementnotif_08122016.pdf

²http://www.mca.gov.in/Ministry/pdf/compromisesrules2016_15122016.pdf

Open ended provision for becoming majority shareholder

The acquirer entity or any person acting in concert with such acquirer can become a majority shareholder to the extent of at least 90% of the issued equity share capital by way of:

- (i) an amalgamation,
- (ii) share exchange,
- (iii) conversion of securities or
- (iv) *any other reason*,

may notify the company of their intention to buy the remaining equity shares. The aforesaid provision has been kept open ended for the majority shareholders to increase their stake to 90% in the transfer company. Besides the options of amalgamation, share exchange, etc the acquirer can undertake any other possible mode to increase its stake to a minimum of 90% for going ahead with the exercise of acquiring minority shareholding.

Determination of Exit Price

Section 236(2) of the Act provides for a pre-determined exit price to be offered to the minority shareholders to be calculated by a registered valuer in accordance with Rule 27 of the CAA Rules, 2016 which provides for evaluation criteria for listed companies as well as unlisted companies.

To proceed with the purchase of minority shareholding, the majority shareholders are required to deposit an amount equal to the value of shares to be acquired by them of the minority shareholders in a separate bank account which shall be operated by the transferor company for atleast one year for payment to the minority shareholders, however, such amount shall be disbursed to the entitled shareholders within sixty days;

Such disbursement shall continue to be made to the entitled shareholders for a period of one year, where the entitled minority shareholders have failed to receive or claim payment arising out of such disbursement.

***Suo moto* offer by the minority shareholders**

The minority shareholders can *suo moto* provide offer to the majority shareholders to purchase their equity shareholding under Section 236 (3) of the Act at a price arrived in accordance with the aforesaid CAA Rules, 2016.

Issue of duplicate share certificates in lieu of undelivered minority shares

In case the minority shareholders whose shares are intended to be bought fail to tender their shares within the specified time period decided by the transferor company, such shares shall be taken as cancelled and the transferor company shall be authorized to issue shares in lieu of the cancelled shares and complete the transfer by following the applicable transfer provision and dispatching the amount paid by the acquirer in advance.

Cases where the minority shareholders are not traceable

When the majority shareholder fails to acquire full purchase of the shares of the minority equity shareholders, due to reasons of non-traceability or death of the shareholders, the provisions of this section will still apply to make an offer for sale of minority equity shareholding for a period of three years from the date of majority acquisition or majority shareholding.

Typical negotiation deal

Section 236 (8) of the Act provides for a typical negotiation deal between the acquirer and the minority shareholders. This provision allows the majority shareholders to share the additional compensation paid by them for reaching from a stake of 75% to a stake of 90% in the transferor company with the minority shareholders. This seems to be a protective provision for the minority shareholders.

Continuance of applicability even after delisting

When a shareholder or the majority equity shareholder fails to acquire full purchase of the shares of the minority equity shareholders, then, the provisions of this section shall continue to apply to the residual minority equity shareholders, even though, —

- (a) the shares of the company of the residual minority equity shareholder had been delisted; and
- (b) the period of one year or the period specified in the regulations made by the Securities and Exchange Board under the Securities and Exchange Board of India Act, 1992, had elapsed.

Broad demarcation between section 235 and 236 of the Act

Sr. No	Basis	Section 235 of the Act	Section 236 of the Act	Remarks
1.	Applicability	Applicable in case of acquisition of shares in a company by another company.	Applicable in case of acquisition of shares of the minority equity shareholders by the majority shareholders, i.e. acquirers along with person acting in concert, persons or group of persons.	Section 235 covers inter-corporate transfers while section 236 includes acquisition by any person, group which also includes any corporate shareholder of the company.

Sr. No	Basis	Section 235 of the Act	Section 236 of the Act	Remarks
2.	Involvement of Scheme	Scheme or contract is involved.	Scheme or contract id not involved	Section 235 involves a lengthy process for buying the shares of minority whereas section 236 is comparatively faster.
3.	Competent Authority	Hon'ble National Company Law Tribunal is the competent authority	No such competent - authority is explicitly involved.	Explicitly section 236 does not provides for an application to be made to the Hon'ble Tribunal unlike section 235, however, in case the minority shareholders comply with the pre-requisites of filing, they may do so.
4.	Period for which money is to be kept in the bank account	No explicit time has been mentioned to keep the consideration payable to the minority shareholders.	Time period of atleast one year has been provided for in the section.	Both the sections fail to mention the maximum time period for which the consideration shall be kept for in the separate bank account, however, considering the provisions of the Limitation Act, such amount should be kept for a maximum time of 3 years.
5.	Role of the company	Company has fiduciary role to play in keeping the	Transferor company only has a role to play that of a	Company has a greater role to play under the provisions

Sr. No	Basis	Section 235 of the Act	Section 236 of the Act	Remarks
		funds in the separate bank account opened for the said purpose.	transfer agent and for taking delivery of the shares and delivering such shares to the majority.	of the first mentioned section than under section 236 of the Act.

Purchase of minority shareholding- *International scenario*

The concept of minority squeeze out is present in many nations and it seems that India has adopted this concept in the like manner. We have discussed the prevalent provisions around the globe with respect to the said concept around the globe.

United Kingdom³

The concept of squeeze out is prevalent in UK. The squeeze out of minority shareholding⁴ can be exercised by two ways as per the provisions of the Companies Act, 2006 (“CA 2006”) of UK. These are through: - (i) takeovers and (ii) scheme of arrangement. We will briefly discuss the first method.

i. Squeeze out by takeovers

The statutory provisions are contained in part 28 chapter 3 of the Companies Act, 2006 (“CA 2006”) dealing with “*Squeeze-out*” and “*Sell-out*” in the context of takeover offers.

“Squeeze out” rights enable majority shareholders to acquire the shares of minority shareholders by purchasing their stake following a successful takeover bid whereas “Sell out” rights enable minority shareholders, in the wake of such a bid, to require the majority shareholders to purchase their shares.

The following measures are imperative for the “Squeeze out” process by takeovers:

- **Takeover Offer-** Under section 974 of CA 2006, a ‘takeover offer’ means an offer to acquire all the shares in a company or where there is more than one class of shares in a company, all the shares of one or more classes.
- **Acquirer (including any associate of the acquirer) to hold atleast 90%-** Squeeze-out rights can be exercised only the if bidder/acquirer has acquired or has unconditionally contracted to acquire:
 - a. At least 90% in value of the shares of any class to which the offer relates; and

³http://www.legislation.gov.uk/ukpga/2006/46/pdfs/ukpga_20060046_en.pdf

⁴ [Guide on Squeeze out- IBA Corporate and M&A Law Committee, 2014](#)

- b. Where the shares of that class are voting shares, not less than 90% of the voting rights carried by those shares.
- **Notice to minority shareholders-** Notice to minority shareholders in the prescribed form, to be served personally or by post and complying with the Companies (Forms) (Amendment) Regulations 1987, must be sent out informing them about the compulsory acquisition of their shares in case of the 90 per cent threshold is reached by the bidder. Serving of the notice entitles the acquisition of shares as per the terms of offer. It is taken to be a criminal offence under the UK laws if the bidder fails to send notice to the minority shareholders.

UK laws are slightly different from that of the Indian provisions with respect to the squeezing out provisions, in terms the time period, giving of notice, etc.

The United States of America⁵

Somewhat similar provisions are also there in USA as one of the structures to assist the majority shareholders squeeze out the minority shareholders. It is one of the forms of short form mergers⁶. Acquirers holding 90% or in some states even 85% of the shares in the target company can offer to buy the shares of the minority shareholders without taking the approval of any other shareholders.

Such minority shareholders have the right of appraisal under which they can go the appropriate authority to challenge the price paid to them for selling their shares to the acquirer. Even after the appraisal process has started the implementation of the short form merger will not get delayed. The acquirer will own 100% of the target company, however the same shall be subject to litigation over the aptness of the price paid in the short-form merger. Also as a general matter, shareholders who accept a tender offer are not entitled to claim that the price offered in the tender offer was too low.

Norway⁷

Under the Norway laws, if the acquirer holds more than 90% of the shares in the target company carrying corresponding proportion of the voting power, the acquirer has the right to acquire minority shareholdings on a compulsory basis. Similarly, the minority shareholders have the right to demand that the acquirer to make compulsory acquisition of its shareholding.

⁵<http://www.ibanet.org/Document/Default.aspx?DocumentUid=1A397D43-8352-4BF4-B382-3C1CF7C83B90>

⁶ [Takeover Guide-United States of America](#)

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https://www.oslobors.no/ob_eng/obnewsletter/download/20fd77664bccdf3f6b8cb0dc95eeb7bb/file/file/Norwegian%20Public%20Limited%20Liability%20Companies%20Act.pdf

Minority shareholders cannot object to such squeeze-out operation being implemented, however they can go against the share price being offered in the squeeze-out. If the price per share is not accepted by all minority shareholders then an independent valuation can be requested by them, usually held at the acquirer's expense.

Singapore⁸

The Singapore provisions in case of squeeze out of minority shareholders is like that of the provisions of section 235 of the Companies Act, 2013 wherein a scheme or arrangement is involved and not that of section 236 of the Companies Act, 2013.

Canada⁹

Section 194 of the Canada Business Corporation Act, 1985 provides for that in case of squeeze out provisions, approval of each class of shareholders will be required who will be affected by such a transaction by way of an ordinary resolution.

Australia¹⁰

In Australia, under the Corporations Act, 2001 there are two methods of squeeze out¹¹

- i. Compulsory acquisition following a takeover bid or
- ii. Compulsory acquisition in other circumstances.

Here, again the threshold limit for squeezing out minority shareholders is 90%. In both these methods, the minority shareholders have the right to object to the acquisition of their securities by signing an objection form (which accompanies the notice served to them) and return it to the shareholders (90%) who approved the acquisition.

The 90% shareholders lodge the objection with the Australian Securities & Investments Commission ("ASIC") along with a list of shareholders who objected.

Once the minority objection is cleared, the compulsory acquisition proceeds if the shareholders in each class who have objected to the acquisition together hold less than 10% of the shares or the Court has approved the acquisition based on fair value for the securities offered.

⁸<http://statutes.agc.gov.sg/aol/search/display/view.w3p;ident=579244a5-83c6-46cc-8563-e01eee5ff6a8;page=0;query=DocId%3A%22c3063e4b-61ed-4faf-8014-fabd5b998ed7%22%20Status%3Ainforce%20Depth%3A0;rec=0#legis>

⁹<http://laws-lois.justice.gc.ca/eng/acts/C-44/page-32.html#h-24>

¹⁰http://www.austlii.edu.au/au/legis/cth/consol_act/ca2001172/

¹¹ [Australia Squeeze out Guide- IBA Corporate and M&A Law Committee 2010](#)

Conclusion

As there was no corresponding provision in the erstwhile Companies Act, 1956, section 236 of the Companies Act, 2013 brings the Indian corporate environment in alignment with the global corporate world by introducing the concept of “squeezing out of minority shareholding”. It can be seen as a progressive move for growth and avoidance of controversial barriers.

However, there can be several lapses observed in the provisions of section 236 of the Act relating to purchase of minority shareholding as to no clarity on whether minority shareholders are bound to accept the offer as it poses a serious threat on the rights of minority shareholders. If the same is interpreted as a compulsory acquisition, there is no scope for opposition by the dissenting shareholders. In addition to this there is no provision for holding a separate meeting of the minority shareholders to vote against such squeeze out. The provisions of section 236 clearly incorporate the concept of “Squeeze out” prevailing in various countries but with certain gaps in the statute for the above-mentioned issues, the practical implication of this section shall act as a fulcrum in deciding the benefits and hindrances it would create in the coming corporate future.

**FAQs on squeezing out of minority can viewed [here](#)
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