

CHAPTER FIVE

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CASE OF THE L & T TAKEOVER

The beauty of corporate control lies in holding the fraction of ownership and enjoying the total ownership over corporate resources. This chapter explores various dimensions of competition for corporate control and leverage of various interacting parties in market for corporate control in Indian corporate scene based on the takeover attempts on Larsen & Toubro Ltd. ("L&T"¹) by the House of Ambanis ("Ambanis"²).

The L&T takeover case, a three year long tussle of corporate control, enveloped in itself host of unresolved features and problems existed in Indian market for corporate control. It had been decisively affected by its ownership (shareholding) pattern, changes in environment through amendments in legal provisions, succession problem in the company, quarreling leadership, submission to White Knight, strategic factors for alliances, corporate rivalry, fair and foul play in proxy contest, raiding by Non-Resident Indian, strategic ploys of holding registrar of members and company secretary in target company, change in attitude of FIs due to change in the Government at the center, supremacy of board of directors over the general body of shareholders, consolidating the control and exhausting the existing and potential resources of the target by innovative public issue and other contracts with target etc. These considerations make this takeover case a unique and appropriate case for in-depth study of Indian

market for corporate control.

This chapter is divided into five parts. Part one sketches the broad functioning of market for corporate control by narrating the role of various participants and discusses the effect of their performance. In particular, an attempt is made to analyse the role of public financial institutions ("FIs"³) in the corporate takeover process. Part two gives the profile of the target (L&T) and the bidder (Ambanis) companies to provide a backdrop to their inter-play in wresting the corporate control. It is followed by a brief account of corporate rivalry between Ambanis and Nusli Wadia and the reported consequences thereof. Part three attempts to unfold the causes which led the Ambanis to takeover the reins of L&T and expounds the underlying motivations which guided them unrelentlessly to consolidate their control over L&T. Part four narrates various twists and turns and related issues in L&T takeover efforts in two phases. Phase one narrates the entry and the exit of Ambanis from L&T; discusses the major issues involved regarding the route adopted by Ambanis to enter L&T; assesses the role played by FIs in inducting Ambanis in L&T and removing them from L&T; and exposes the inefficiencies of legal provisions to justify their obsolescence and indolence. Phase two relates to the post exit happenings and the determined but unsuccessful attempt by Ambanis to regain control over L&T through unprecedented historical proxy collection drive besides discussing the indecisive stand of FIs and debilities of legal provisions encountered by parties involved in the

TAKEOVER ATTEMPTS ON L & T

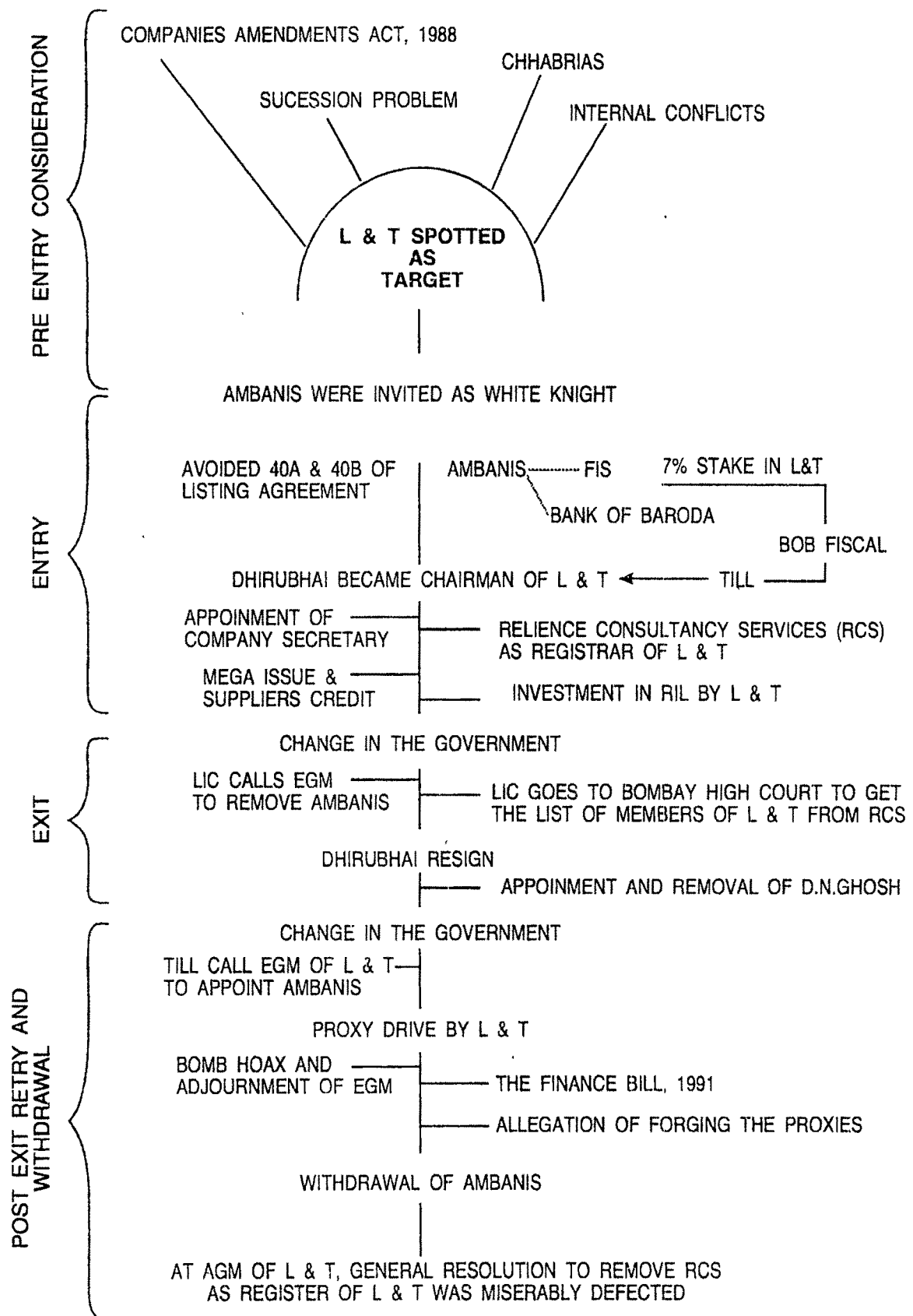
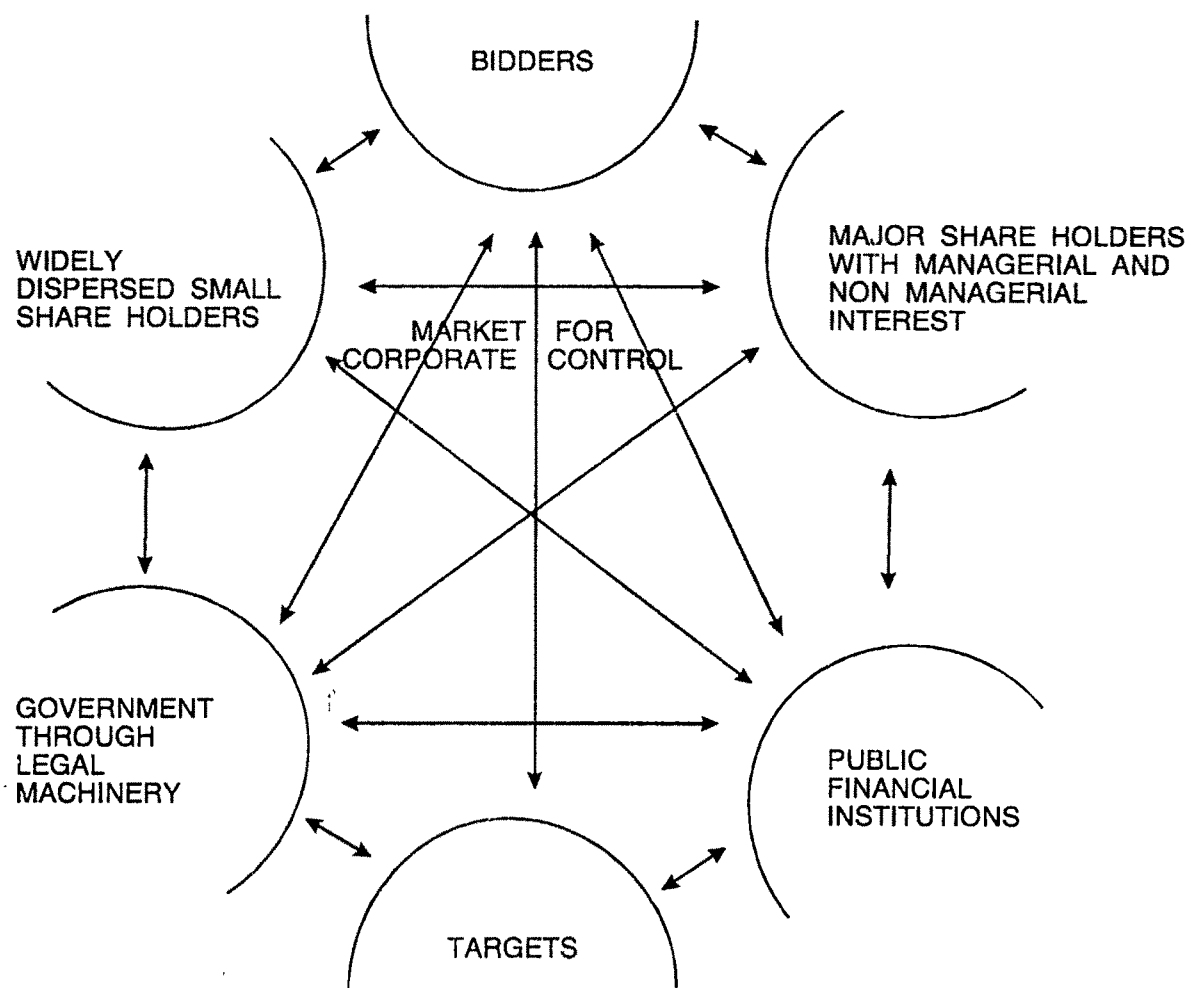


Fig. 5.1

takeover. Part five summarises, the major policy issues necessary for efficient functioning of market for corporate control, and in particular, the issues raised by this case. A panoramic view of takeover attempts on L&T is given in Fig. 5.1.

5.1. THE MARKET FOR CORPORATE CONTROL

For stock market to serve as efficient market for corporate control it should be sufficiently efficient in pricing its securities and perfect in its various technicalities. How efficiently Indian stock market performs its role as a market for corporate control is an unanswered question in the annals of researches in Indian corporate finance. A typical market for corporate control is a place where rival managements compete for controlling stake⁴. Extending it to Indian corporate scene, it is a place of continuous interactions among the bidders, major shareholders like institutional investors, and existing management and their supporters having substantial equity stake in the company, large number of minority shareholders widely dispersed across the country, and finally the Government monitoring the market through its legal machinery to protect the large number of small shareholders and to maintain the integrity of the market and transparency of transactions. The various parties involved in the game of the corporate control is shown in Fig. 5.2.



PARTICIPANTS IN MARKET FOR CORPORATE CONTROL

Fig. 5.2

5.1.1. The Market Participants

The magnitude and the quality of participation of these players decide the efficiency of market for corporate control. Firstly, the bidder is one of the major interacting parties in this market. It is spotting and stalking the "right" target and observance of regulatory provisions in letter and spirit and making relevant disclosures in time make the functioning of the market more efficient. In contrast, taking over the company in collusive negotiated deals along with the assured institutional support by beating the rules of the game, exploiting the existing weaknesses and debilities of the market and squeeze the target only for their own benefit may undermine the confidence of the participants of the market. A healthy competition among the bidders certainly improves the efficiency of the market but corporate rivalry beyond certain extent will cost the market and its participants instead of benefiting from the takeover process.

Secondly, business families having substantial holdings with or without managerial interest is another group in the company that plays vital role in the market. The Indian corporations are dominantly family controlled corporations all along their growth and development⁵. These families have been maintaining their control through the support of FIs, inter-corporate investments, investment through trusts; besides, the uncommitted and widely dispersed 'impersonal' investors⁶ assured them of their position and prestige. As family grows bigger, the conflict to head the companies

culminates in partitioning of various family owned corporate properties⁷. This, at times, observed to have resulted in transfer of corporate control outside the market without giving any opportunity to small shareholders to tender their shares at negotiated price. This may frustrate the interplay of free market forces.

Thirdly, the large number of small shareholders, if participate effectively, can also play the decisive role in the market by bringing in and thrashing out the target companies from the market by pricing them efficiently. They have a special role to play in public tender offer and proxy contest where they get "real" chance to appoint their agents. In contrast, if they get lured away by disproportionately high attractive offer⁸ or high premiums for endorsing the proxies⁹, they may contribute in prolonging the immaturity of the market.

Fourthly, the Government through its legal arm enter the market¹⁰. The law aims at protecting the target from unscrupulous bidders, safeguarding the interests of small shareholders by enforcing the bidder to make offer to buy the shares at a price offered in the negotiated deal, restricting the unconditional discretion of the target management to refuse the transfer of shares to protect their controllership, and monitoring the privately negotiated deals of share transfer by major shareholders. Hence, the basic intention of the corporate law is to protect the integrity of the market from those who seek to abuse its freedom.

Finally, the FIs as holder of substantial equity play a decisive role¹¹. They, on the account of their shareholdings nominate directors on the board of the companies. Their decisions to participate or to remain neutral in any takeover battle may decide the ultimate control of the target company. An independent decision on their part, but in the interest of the company and the public is expected to improve and infuse healthy competition in the market.

5.1.2. Role of Financial Institutions

Historically, the role of FIs has been conceived as bridging the "gap" the promoters is unable to finance - essentially a lending function. After Second Five Year Plan, the development planning changed the concept of industrial financing by FIs¹². Their major task was envisaged as mobilising the maximum savings of the economy and ensuring its distribution over different sectors of industries according to planned priorities¹³. Accordingly, the Government assigned the role of intermediation to Life Insurance Corporation (LIC) of India and Unit Trust of India. Their role was partially to fund the needs of Development Financial Institutions and to invest directly or indirectly in primary as well as secondary capital markets¹⁴. This policy initiative had led FIs to have garnered sizable equity holdings in private sector companies on account of underwriting agreements, exercise of convertibility options, preferential allotments besides, active participation in secondary capital market¹⁵.

The guiding investment policy of these investment institutions was to safeguard and promote the interest of their policy/unit holders. Besides, their investment policy should serve the larger economic and social considerations beneficial to the country¹⁶; they should "act purely on business principles with priority being given to public interest"¹⁷ and without assuming the role of operator or speculator, acquire the control or participate in the management of any concern in which it has an interest as an investor. In fact as a major equity shareholder in private corporate sector their role is to promote greater discipline among the corporate managements adding a new dimension to public control of private enterprises¹⁸.

Acceptance of recommendations of Dutt Committee, 1969¹⁹, gave a major break to the role played by the public financial institutions in private corporate sector. Adoption of the concept of joint sector and compulsory convertibility clause as recommended by the Committee envisaged the role of financial institutions as: (i) to share the benefits accruing from projects assisted by public financial institutions, and (ii) to participate in the management of assisted companies.

This led to compulsory nomination of directors on the board of assisted/interested companies and redefined their role in various existing companies. Nominee directors were made obliged not only to safeguard the interests of the financial

institutions they represent but also to serve the interests of sound public policy²⁰. Their role was envisaged as to prevent "concentration of economic power" and to ensure that public interest and not merely private profit would guide the operations of companies in private sector ²¹. These directors should keep themselves fully acquainted with the affairs of the assisted companies to make institutional participation at policy level, a meaningful reality.

"Any abuse of its powers and privileges by the existing management/promoter group and any pursuit of policies detrimental to the interest of the company such as questionable diversion of funds in or lending to other companies in which controlling group may be interested, should as far as possible prevented by nominee directors"²².

Not only that,

"...they should ensure that the tendencies of the companies towards extravagance, lavish expenditures ... are curbed"²³.

It follows that equity holdings of various public financial institutions should be effectively used for enlarging the role of the "State" in the management of private sector companies²⁴.

In market for corporate control, FIs, through their nominee directors, have been observed to have participated in three ways. Firstly, by participating constructively in boardrooms in electing the controller of the company. Here, they may support the nominee of either the existing management or competing management; they may also resume the reins of company by rejecting both existing or competing management.

Secondly, by remaining neutral and allow the remaining shareholders to decide the controller of the company. Thirdly, by participating in capital market, directly or indirectly, they may facilitate the transfer of control by selling the substantial equity stake (generally a decisive one) in target company to the competing management in the market or in a collusively negotiated deal.

In the attempted takeover of Escorts Ltd.²⁵, FIs have reportedly assisted the corporate raider by calling an extraordinary general meeting (EGM) to remove the team of existing management. Similarly, FIs assisted the competing management in Shaw Wallace Ltd., Manglore Chemical and Fertilizer Ltd., Coromandal Fertilizer Ltd. While in the cases of Carbon Corporation Ltd., Modi Rubber Ltd., and L&T Ltd., FIs have supported the existing management and aborted the raid by competing management to takeover the company. On the contrary, on one hand, there are many cases of corporate battles, for example, Ashok Leyland Ltd., Assam Tea Ltd., Dunlop(India) Ltd. where the FIs remained neutral and refrained from voting on issue of corporate control and on the other, there are cases such as Swadeshi Polytex Ltd., Shaw Wallace Ltd., Premier Tyres Ltd., S&S Power Ltd., where the FIs did not hesitate to takeover the reins of the company in their hands removing both the existing as well as competing management.

Though the Supreme Court had in a historical takeover case of Escorts Ltd., crystallised the position of FIs as a

shareholder in private sector companies by refraining to examine the actions of State or instrumentality of State in private law field. Clarifying further the status of FIs, particularly, in an action of transferring corporate control, Justice Chinnappa Reddy observed that

" When State or instrumentality of State ventures into corporate world, and purchase the shares of the company, it assumes to itself the ordinary role of shareholder and dons the robes of shareholder with all rights available to such shareholder"²⁶.

Thus, in a competition for corporate control in boardrooms of listed companies, the role of FIs have been changing devoid of consistancy. It heralds a fragile transition from their role as a catalyst to an activist in private sector which has brought many brickbats instead of bouquets.

The participation of FIs in capital market also, especially in secondary market, has not been without controversies. In the case of takeover attempt on India Cements Ltd., where the FIs had supported the raider ITC Ltd., by transferring their controlling equity stake in India Cements Ltd., to former in a collusively negotiated deal. The issue created a strom in corporate boardrooms about the role of FIs in secondary market during the corporate battles. The controversy led to the introduction of Clause 40 A and 40 B in Listing agreement. The similar story was repeated in the case of L&T Ltd.²⁷ The Supreme Court has severly criticised the role of FIs in secondary capital market in the context of corporate takeover battles and cautioned that

"...the public financial institutions should be very prudent and cautious in transferring the equity shares held by them not only being guided by the sole consideration of earning profit by selling them but by taking into account also the factors of controlling the finances in the market in public interest. The public financial institutions while transferring or selling bulk number of shares must consider whether such a transfer will lead to the acquisition of a large proportion of the share of a public company and thereby creating a monopoly in favour of a particular group to have a controlling voice in the company if the same is not in the public interest and not congenial to the promotion of business "28.

The FIs have yet to convince the corporate boardrooms that their decisions on takeover contests are governed by the public interest/shareholders interest and not directed by the supremacy of any invisible hand.

Thus, the emergence of the financial institutions and their venture to finance the private corporate sector has brought to surface the multifaceted complexities of intervention of State in private field of market for corporate control. Though their fragility in corporate battles are getting crystallised over a period of time learning from the experiences; still, the unresolved issue, interesting to observe in time to come, is how the FIs, as a major shareholder and an extended arm of State in the private sector companies, ensure transparency of deals in the market and promote greater discipline in the corporate boardrooms.

5.2. A BRIEF PROFILE OF THE TARGET AND THE BIDDER COMPANY

This section portrays operational and financial profile of the target and the bidder companies to provide a backdrop for the discussion of the inter-play of the L&T and Ambanis in wresting corporate control along with critical analysis of corporate rivalry between Ambanis and Nusli Wadia.

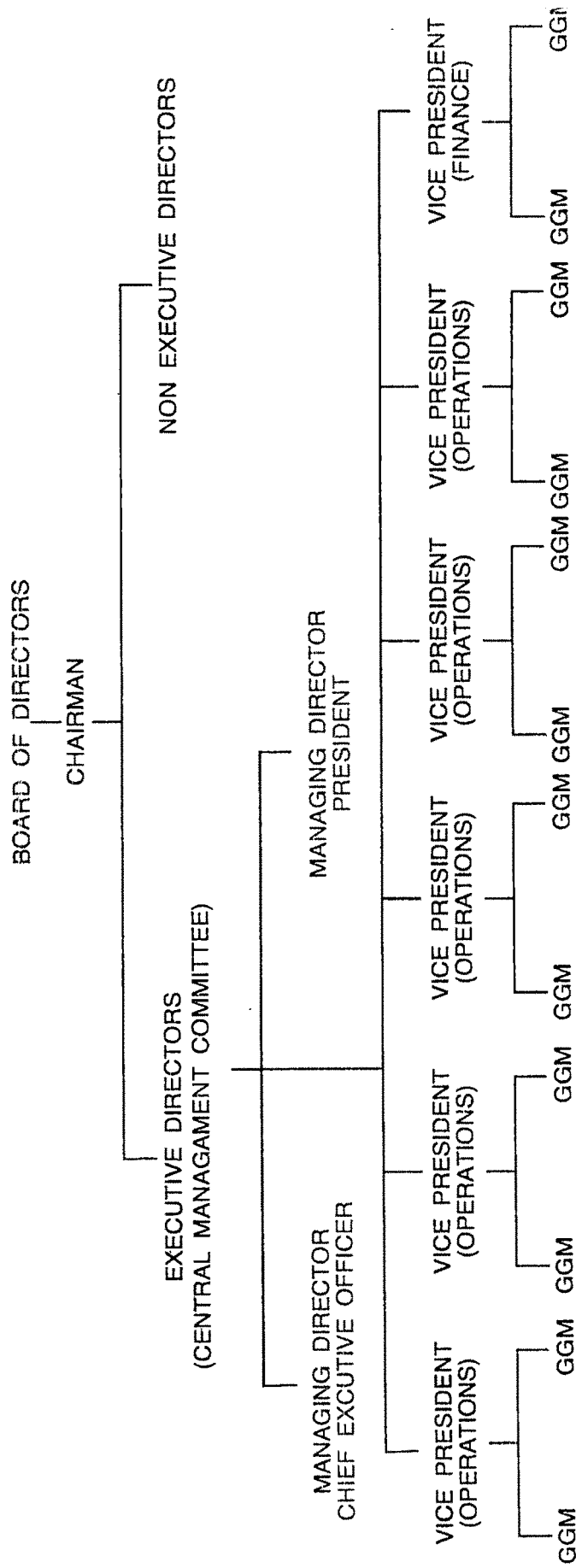
5.2.1 The Target Company: Larsen & Toubro Limited

In 1938, the company was a partnership firm of two Danish Engineers, H. Holck Larsen and S.K. Toubro. It was incorporated as a private company in 1946 under the Indian Companies Act, 1913. Later in 1950, it was converted into a public limited company. Started as small engineering firm, L&T is at present India's widely diversified company having 12 different business groups with a turnover of more than Rs.2000 crores, and expecting to cross Rs.10,000 crores in the next seven years. With a net worth of Rs.1420 crores, uninterrupted dividend payment for last 38 years, rewarding the shareholders with six bonus and sixteen rights issue, having enrolled more than ten lakhs shareholders, it enjoys blue chip status among investors community.

Organisation Profile

The company is controlled by the Board of directors consisting of 21 eminent professionals, industrialist and administrators. Out them eight are whole time directors and remaining 13 are part-time directors. The board is headed by

ORGANISATION CHART OF L & T LTD.



GGM = GROUP GENERAL MANAGER

Fig. 5.3

the chairman and day-to-day management of the company is handled by its two managing directors (MD) namely, U.V. Rao, MD and Chief Executive Officer and S.R.R. Subramaniam, MD and President. They are assisted by 5 Vice Presidents of Operations and one Vice President of Finance and Operations. They are in turn helped by Group General Managers of respective Group of services provided by L&T. The organisation chart is given in Fig. 5.3. Surprisingly, there is no separate whole time director as vice-president for vital areas of company's thrust like Human Resource Development or Marketing. The nine executive directors namely, one Chairman two managing directors and six vice presidents form a Central Management Committee (CMC) which meets weekly at its Bombay head office, to review the progress of the company.

During last three years, there has been many upheavals in the board of L&T. Before the first takeover attempt the board was headed by Chairman N.M. Desai. After his retirement in 1988, Dhirubhai Ambani became Chairman of L&T in April, 1989. Shri Mukesh Ambani was made vice-chairman by creating an additional post. Besides, B.L. Bhakta and A.D. Ambani, nominees of Ambanis, were appointed as part-time directors on the board. But in April, 1990, soon after the change in the Government in the Parliament late 1989, D.H. Ambani quit L&T by resigning as the chairman of the company and M.D. Ambani resigned from post of vice-chairman but remained a part-time director of the company. Consequently, D.N. Ghosh, a nominee of FIs, appointed as Chairman of L&T. Again with

the change in the Government at centre in November, 1990, D.N. Ghosh quit L&T on instructions from the Government in February, 1991. Since then L&T is not having chairman on its board. Although there was frequent upheavals in the structure of whole time directors on the board, still the disturbance did not percolate down to the level of part-time directors. The three nominees of Ambanis are still there along with the nominees of FIs and other eminent professionals. The list of Board of directors before, during and after the tenure of Ambanis in L&T is given in Appendix 5.1.

In a Business world - MARG (Marketing And Research Group) poll on India's most respected company, L&T ranked second in the year 1992. It has been consistently maintaining its rank among top five most respected companies in the last five years. To quote V.V. Rao "the strength of L&T lies in its people. We have the same people that others do. Nor are we the best pay masters. Yet, they perform so well because the L&T provide unique work culture". There exist an unique Employee's Suggestion Scheme at L&T. It receives over 1200 suggestions received every year. They help to reduce costs, step up productivity, achieve higher standards of quality, introduce better safety measures, improve housekeeping.

Operational Profile

The operations of the company are divided into twelve business groups (refer total activity portfolio of the company in Table 5.1) spread across the world. They are carried out at eleven different workshops located across the

country and with the help of four subsidiaries and two associated companies. The main objective of the company are to carry out business as civil, mechanical, electrical, chemical and agricultural engineers; as manufacturers; as importers and exporters and as contractors.

Group Businesses: Group one covers four businesses. Firstly, manufacturing of earth moving, road making equipment and construction. L&T pioneered the manufacture of hydraulic excavators in India in collaboration with POCLAIN S.A. of France. A wide range of construction equipment such as crawlers, loaders, trenchers etc. are manufactured in collaboration with JI Case; U.S.A. Secondly, it also manufactures a wide range of hydraulic equipments in collaboration with Suaer Sunstrand, U.S.A. Thirdly, it offers drilling equipment, accessories and services for oil exploration and production, on land and off-shore in collaboration of world renowned manufacturers. Fourthly, L&T represents Detroit Diesel Corporation, U.S.A. for its entire range of DDC diesel engines in India.

Group two covers eight business. Firstly, it designs and manufactures of plant and equipment for the chemical, petrochemical, petroleum, fertilizer and synthetic fibre industries to customers' specifications and international codes. For this, it has collaborated with Struthers Wells Corporation, U.S.A., Babcock Enterprise, France, Japan Steel Works, Japan, Man-Gbh, Germany. Secondly, it also offers full range of oil and gas equipment and systems in collaboration

with Rauma, Finland; Petrolite, U.S.A.; Boliden, Sweden. Thirdly, it offers power plants including co-generation captive power plants on a turnkey basis including design engineering, erection and commissioning, in connection with Cockerill Mechanical Industries, Belgium.

Table 5.1

Portfolio of Business Activities of L&T Ltd.

GROUP	ACTIVITIES
Group I	Construction, earth moving & road making equipments
Group II	Projects: Chemical unit equipments Oil & gas Cement machinery Food processing machinery Thermal power Fabrication: Capital goods manufacturing
Group III	Switchgear Contracts
Group IV	Eutectic, products & processes, packaging, and valves & equipments
Group V	Cement
Group VI	Rubber processing machinery and plastics
Group VII	Shipping
Group VIII	Software Consultancy
Group IX	Merchant Export
Group X	Consultancy and engineering services
Group XI	Control and automation, data products, medical eqpts. telcom, and process instruments
Group XII	Construction: (E C C) Civil, mechanical and electrical

Source: Business World, Aug-Sept, 1993

Fourthly, it manufactures, in collaboration with FL Smidth & Co., Denmark, Cement machinery, mineral processing kilns and calciners. Fifthly, it undertakes designing to commissioning of plant and equipment for large automated dairies, breweries and other food processing businesses in collaboration with Atlas Industries, Denmark; West Falia, Germany; Buss AG, Switzerland; Nu-Con Ltd., New Zealand; Goudsche, Holland. Sixthly, it manufactures critical equipments and systems for nuclear, thermal and cogeneration plants; space projects and defence in collaboration with Foster Wheeler, U.S.A.; Stork Boilers, Netherlands. Seventhly, it supplies complete plants and systems on a package as well as on a turnkey basis for diverse operations of chemical process and allied industries. For this, it has collaboration with Swenson process equipment Inc., U.S.A.; Zimpro Passavant Inc., U.S.A.; Noell-lga, Germany; John Zinc, U.K., etc.

Group three is engaged in the manufacturing of custom-built switch gear products and related accessories and petrol pumps. It is India's largest manufacturer of low tension switch gears.

Group four is engaged in four different business. Firstly, it markets a range of sophisticated application engineered Eutectic Welding Alloys and patented processes at its subsidiary EWAC Alloys Ltd. Secondly, it markets Powder Metallurgy (PM) high speed steel tools and dies at its EWAC Alloys Ltd., in collaboration with Castolin Eutectic International, S.A., Switzerland. Thirdly, it manufactures

varieties of quality bottle closures and are exported to Africa, Middle East and South East Asia. Fourthly, it also markets wide range of industrial valves, assessories and equipments at its associated company Audeo India Ltd., in collaboration with Idro Sapiens, Italy, Advanced Products, Belgium; Jansen GmbH Germany.

Group five is responsible for the manufacturing and marketing of the cement. It has started with installed the capacity of 1.1 million tonnes per annum in 1983, by 1994 it will have the capacity of nearly 6 million tonnes per annum. The plants are computerised and controlled from central control room.

Group six is responsible for two kind of businesses. Firstly, in rubber processing machinery, it supplies automotive tyre and tube, tyre retreading with rubber processing machinery manufactured by L&T's subsidiary, L&T-McNeil Ltd., Madras. For this business, it has collaborated with Arkon Standard, U.S.A.; Mitsubishi Heavy Industries, Japan; Maskin Fabrikein SIO, Denmark. Secondly, in plastics processing machinery. It supplies a range of injection moulding machines and systems for processing of thermoplastics and thermosets. They are manufactured in collaboration with Mannesmann Demog Kunststofftechnik, Germany.

Group seven is engaged in shipping business L&T's shipping fleet comprises six modern dry bulk ships which have been built at Japanese shipyards to high technical specifications. It is managed by L&T's shipping group at Bombay.

Group eight deals in software consultancy. It offers both onsite and offshore software consultancy services in areas of custom made software development and software conversion and design.

Group nine is recognised Export House and covers mainly two businesses. Firstly, in merchant exports, L&T's marketing network provides global access to Indian manufacturers in small and medium sectors. Secondly, in footwear business, the Kalol unit manufactures various types of footwear for quality conscious markets of U.S.A. and Middle East countries.

Group ten comprises of seven more business. Firstly, L&T, being backed by years of experience in various fields, offers technical consultancy and project engineering services to several Industries. Secondly, also undertakes design, manufacture and supply of wagon handling and marshaling systems in collaboration with Strachan & Henshaw, U.K. Thirdly, it has specialised in the manufacture of integrated iron and steel works and hydel plants. Fourthly, it manufactures plant and equipment for material processing like mineral bifurcation, agglomeration and pelletisation, in collaboration of Sala International AB Sweden. Fifthly, it manufactures machinery and equipment for pulp, paper and board mills in collaboration with J.M. Voith GmbH, Germany. Sixthly, it designs and manufactures an exhaustive range of size reduction equipment to cater to the needs of various Industries like - coal, cement, steel, power, etc. in

collaboration of Hazemag GmbH, Germany. Seventhly, in foundry and furnace business it manufactures Industrial castings in the iron and steel range, in collaboration with Consarc Engineering Ltd., Scotland.

Group eleven is engaged in electronic and allied business and covers six businesses. Firstly, in control and automation section, it manufactures electronic control systems for core industries in collaboration with Jeumont-Schneider, France; and Yaskawa Electric, Japan. Secondly, it manufactures wide range of Computer peripherals which includes D.M. printer, Laser printers, Floppy Disk Drives, Hard Disk drives etc. Thirdly, it manufactures wide range of medical equipments in collaboration with Biocadio Biomedica, Italy; Kontron Instruments, U.K. Fourthly, in telecommunication business, its manufacturing abilities ranges from subscriber terminal equipment to public switching system upto 10,000 lines capacity. Fifthly it manufactures wide range of process test & measurement instruments at its subsidiary L&T-Gould Ltd. and its associate Audco India Ltd. in collaboration with Teledyne Farris Engineering, U.S.A.; Gould Inc., U.S.A. and many other world known manufacturers in this field.

Group twelve is a construction group widely known as Engineering Construction Corporation (ECC). It offers turnkey services in civil, mechanical and electrical engineering to projects in India and abroad. In civil business, it has seven specialised areas of operation, namely, Power projects, Industrial projects, Building and system Housing, Maritime

Structures, Bridges and Highways, Foundation engineering and Earth moving and irrigation projects (for example, the Baha'i House of Worship, New Delhi). In mechanical business, it caters vital services to thermal, nuclear and gas based power plants, petrochemicals, refineries and fertiliser plants, cement, steel and other metallurgical projects, and ports and harbours. The Vishakhapatnam Steel plant and 275 metre high RCC chimney of Anpara Thermal Power Station, U.P. confirms the mechanical work of world class. Its electrical division undertakes electrification of major power plants, fertilizer and petrochemical projects.

Workshops: L&T has eleven workshops across the country.

Powai: It is the main workshop of L&T situated at Powai. It comprises the switch gears, electronics and bottle closure factories, heavy and medium fabrication shops complemented by machine shops. It shelters Research and Development activities of various groups. It is also equipped with the latest computer based hardware and software systems and uses the latest management tools for production, planning and control.

Madh: It is located on Madh island in the western suburb of Bombay where wide range of switch gears are manufactured.

Ahmednagar: It is also L&T's one of the switch gear manufacturing plants and its an industrial centre in a backward area of Maharashtra.

Faridabad: It is also a switch gear plant meeting the needs of the Industries in northern region. It specialises in low tension and tailor made switch boards.

Kansbahal: It manufactures plant and equipment for paper, iron and steel, and mineral processing industries, crushers, turbines, material handling equipments, and high quality castings.

Banglore: It is one of the major modern manufacturing facilities centres of the L&T. The complex comprises Machinery works, Hydraulic Works and Engine Export Oriented Unit.

Phithampur: It is located in Dhar district of Madhya Pradesh and meets the requirements of Group one discussed above.

Awarpur: It is India's one of the modern cement plants equipped with a computer based control system. It comprises of two units with capacity of 1.1 million tonnes p.a.

Mysore: This is L&T's modern electronics factory where the computer peripherals and medical electronic equipments are manufactured.

Hazira: It is L&T's heavy engineering complex situated on the bank of Tapi close to Arabian sea, near Surat. It is equipped to manufacture large and heavy equipment for nuclear and thermal power projects, petrochemical and fertiliser industries, aerospace, oil exploration and marine related sectors which can be shipped out via water ways.

Kalol: It is L&T's footwear manufacturing unit and is one of the most modern unit in India, having the capacity to manufacture 6,00,000 shoe pairs per year.

Group Companies: L&T has four subsidiaries and two associated companies in its group.

Subsidiaries

EWAC: EWAC Alloys Ltd. is a joint venture of L&T and EUTECTIC Corporation, U.S.A. It manufactures special purpose, Eutectic welding alloys, torches and allied assessories at EWAC's factory at Ankleshwar.

L&T McNeil: L&T McNeil Ltd. is a joint venture of L&T and McNeil Ltd., U.K., It manufactures a wide range of rubber machineries, type building machines, plastic injection moulding machines and rang of auxiliary equipments at its Powai factory.

L&T-Gould: L&T-Gould Ltd. is a joint venture of L&T with Gould INC. U.S.A. The company has its manufacturing facilities at Mysore. It manufactures wide range of electronic test and measuring equipments.

L&T-NIRO: It is a joint venture of L&T and Niro A/S of Denmark. It manufactures powder processing and producing plants. It is likely to set up modern manufacturing facilities near Baroda.

Associates

Audco: Audco India Ltd., is an associate company with 50% shareholding by BTR plc of U.K. It is India's leading manufacturer of a large variety of industrial valves - the first to be certified under ISO 9001.

TENGEL: It is a joint venture of L&T and caterpillar Inc., U.S.A. It manufactures crawler under carriage systems for excavators and bulldozers.

Activity of vital importance of the country

L&T has been closely involved in the manufacturing of sophisticated equipment for Space, Defence and Nuclear Power related research and programmes. In 1970s, it manufactured India's first indigenous nuclear reactor for Rajasthan Atomic Power Plant and motor casings for Indian Space Research Organisation. In 1980s, it developed the tri-junction welding technique for critical parts of nuclear reactor. It offers a wide range of equipment and fully engineered systems for defence applications. The company has in-house capability for analytical work, design, development and manufacture of sophisticated, and hightech equipment for armed forces. It has collaborated with Foster Wheeler, USA for surface condensers which are vital for space and nuclear programmes.

Awards

For the five years in succession, it had received the Award of Good Industrial Design at Honover Fair, West Germany, for its switch gear products. In 1982, it received the Republic Day Award. In 1987-88, it received the CEI Award for excellence in energy conservation and management. In 1988, it was Awarded for Excellence from Maharashtra Chapter of American concrete Institute. In 1993, U.V.Rao, the Chief Executive Officer and Managing Director was awarded "Chief Executive Officer of the Year" by Pranav Mukherjee, the Deputy Chairman of Planning Commission.

Financial Profile

The company has grown manifold in terms of its networth and turnover since its incorporation. With an initial outlay of Rs.25 lakhs in 1946, it had at the end of 1991-92, a capital of Rs.130 crores with reserves amounting to Rs.747 crores. The company is also known for sharing its prosperity with the equity shareholders. Over a period of five decades, it has declared bonus issues for six times and made rights issue for sixteen times. It has been paying uninterrupted dividends to its shareholders all along its development, in a range of 25 to 35%. Capital structure of the company since its inception is given in Appendix 5.2 and scanning of important financial parameters for the last seven years i.e., from 1983-84 to 1991-92 is given in Appendix 5.3.

The company was incorporated in 1946 with 75,000 equity shares issued to vendors and 51,250 shares issued to Hilde Ltd. In 1950-51, it issued 6,500 Preference shares and 1,35,000 equity shares to the public. Since then, the company has not looked back. Almost every year the company has come out with either bonus or rights issue or convertible debentures. The last right issue of the company was made in 1984-85 in 1:5 at a premium of Rs.50, and bonus issue in 1985-86 in the ratio of 3:5 capitalising the reserve of Rs.5199 crores. On the basis of last seven years statistics from 1983-84 to 1991-92, the Share Capital and Reserves have registered the compound annual growth rate of 23% and 30% respectively. The rate of change in share capital and Reserves were 73% and 66% respectively. In contrast, (in

1990-91 to 1991-92) the borrowed funds have increased only marginally. The compound annual rate for the last seven years has been 12% per annum, and the rate of change in 1990-91 to 1991-92 was in fact negative, namely, -15%. This is also supported by consistently declining debt equity ratio from 1.2 in 1983-84 to 0.2 in 1991-92. The latter is substantially low when compared with industrial average of 1.14. The Total Assets and Net Block of Assets have registered a compound annual growth rate of 20% and 16% respectively as compared to the industrial average of 20%. The funds blocked in working capital at the end of 1991-92 were Rs.554 crores which is growing at the rate of 40% per annum. The current ratio has been observed to have increased all along from 0.9 in 1984-85 to 1.75 in 1991-92 which was marginally lower by 0.03 from industrial average of 1.78 in 1991-92.

L&T has undergone many merging exercises with its subsidiaries and have made them their separate divisions. In 1969, Alu Capsules Ltd. and Indian Crown Cork Ltd. were amalgamated with the company. Few other cases amalgamations with the company were Canara Bank Ltd. in 1972, Wilcox Buckwill India Ltd. in 1979, Utkal Machinery Ltd. in 1981 and Engineering Construction Corporation in 1982.

On operational side, the turnover has increased almost 5 times in the last seven years, from Rs.359 crores in 1983-84 to Rs.1735 crores in 1991-92. The compound annual growth rate of turnover has been 23% as compared to industrial average of 18%. Simultaneously, the profit after tax has been increasing

all along its growth from Rs.23 crores in 1983-84 to Rs.102 crores in 1991-92 with compound annual growth rate of 21% which is all along higher than industrial average. Profit after tax (PAT) to sales has also remained quite stable all along in range of 4% to 6% from 1983-84 to 1991-92. This ratio for the company has remained substantially above the industrial average during the respective years. The industrial PAT to sales is hovering around 3.5%. Return on networth has remained quite volatile in a range of 10% to 18% while industrial average has remained 13.7%. Earning per share, price earning ratio and therefore market price have remained quite volatile. The last seven years average market price has shown increase by more than 330% from Rs.74 in 1983-84 to Rs.245 in 1991-92. On the other hand, rate of dividend has been stabilised in a range of 25 to 35%.

Thus, company has been consistently performing better than an average company in the industry. It has been consistently growing in terms of turnover, profit, networth and total assets. It has been observed to have remained conservative in utilising its debt potential by resorting frequently to retained earnings, equity and quasi-equity capital for financing its projects.

In the last decade the company has frequently resorted to convertible debentures for financing its growth. The series of convertible debentures I, II, III and IV were issued in 1983-84, 1987-88, 1989-90 and 1990-91 and mobilised Rs.960 crores. Of this IVth series convertible debentures of Rs.820

crores issued in 1990-91 had remained quite controversial and had been challenged in the High Court and Supreme Court. Finally, the Supreme Court judgment upheld the mega issue in its original terms.

5.2.2. The Bidder: Reliance Industries Ltd.

Reliance Industries Ltd. (herein after referred as "RIL") has been a phenomenon in Indian corporate history²⁹. The success of RIL rested on a tripod of vision, high technology and superb financial management. Ambani has no fancy of degrees, no genteel affected mannerisms of the latest generation of industrialists nor the technical qualifications of privileged scions. But he had a burning desire to be number one. RIL is Ambani's preoccupation, hobby and passion³⁰.

It had started as a trading concern in textiles by D.H.Ambani, an ambitious son of a school teacher from a small village (Chorwad) in Gujarat. It was incorporated as a private company in 1966 under the banner of Reliance Textile Industries Pvt. Ltd.(RTIPL). Later on, it was in 1975 that the company was converted into a public limited company in 1975. Since then, over a period of time it has become one of the biggest families of shareholders (3.8 million) in the Indian corporate world. It went in for amalgamation with Minylon Ltd. in 1976 and Siddhpur Mills Ltd. in 1981. The latter was then converted into a subsidiary in the name of Devti Fabrics Ltd. In 1985, Reliance Textile Industries Ltd. was changed to Reliance Industries Ltd. In the process of its development it floated four subsidiaries (See Appendix 5.4).

The emergence of Reliance from a small textile concern to the nation's biggest corporate house within a span of less than thirty years, is chronologically given in Appendix 5.5.

Operational Profile

A trading concern started by the Ambanis, it kept on integrating its business through backward integration. It has also diversified horizontally into plastics and detergent intermediaries.

In the first phase of its backward integration, it started manufacturing textiles at its Naroda Plant.

In the second phase of backward integration, it went into manufacturing Polyester Staple Fiber (PSF) and Polyester Filament Yarn (PFY), a raw material for the manufacturing of fabrics, at Patalganga plant.

In the third phase, it went one more step backward by starting the manufacture of fiber intermediate items such as Purified Terepathalic Acid (PTA) and Mono Ethylene Glycol (MEG). It also went in for horizontal diversification to manufacture plastics from the raw materials such as Poly Vinyl Chloride (PVC) and High Density Polythyne (HDFE) and highly demanded detergent raw material, Linear Alkyl Benzene (LAB).

In the fourth phase, it went one more step backward straight to manufacture the basic raw material ethylene by cracking the natural gas under specified conditions.

In the proposed fifth phase, in the last possible step of backward integration, its proposed refinery complex is expected to process petroleum crude to produce kerosene, naphtha, liquified petroleum gas and fuel oil. The process of backward integration and horizontal diversification of RIL is shown in Fig. 5.4. Thus, it integrated right from manufacturing basic raw material naphtha from petroleum crude to textiles.

RIL has three manufacturing complexes. Two of them at Naroda and at Hazira in Gujrat and one at Patalganga in Maharasta. One more refinery complex is proposed near Jamnager in Gujarat. Fig.5.4 sketches the manufacturing of various products at their respective complexes. Naroda has the textile complex, where yarn is processed and synthetic fabrics are manufactured, and it is one of the most sophisticated textile plants in India. It produces wide range of fabrics, like, dress materials, suitings and shirtings under the brand name of "Vimal". At Patalganga, it has fiber and petrochemical complex. It produces polyester fiber intermediaries (PX, PTA, PSF, and PFY) and detergent intermediaries (LAB and Paraffin). Hazira complex has its petrochemical and plastic complex. It manufactures more basic petrochemical compound (EO, MEG, and VCM) and plastic intermediaries (PVC, HDPE, and LDPE). The refinery project

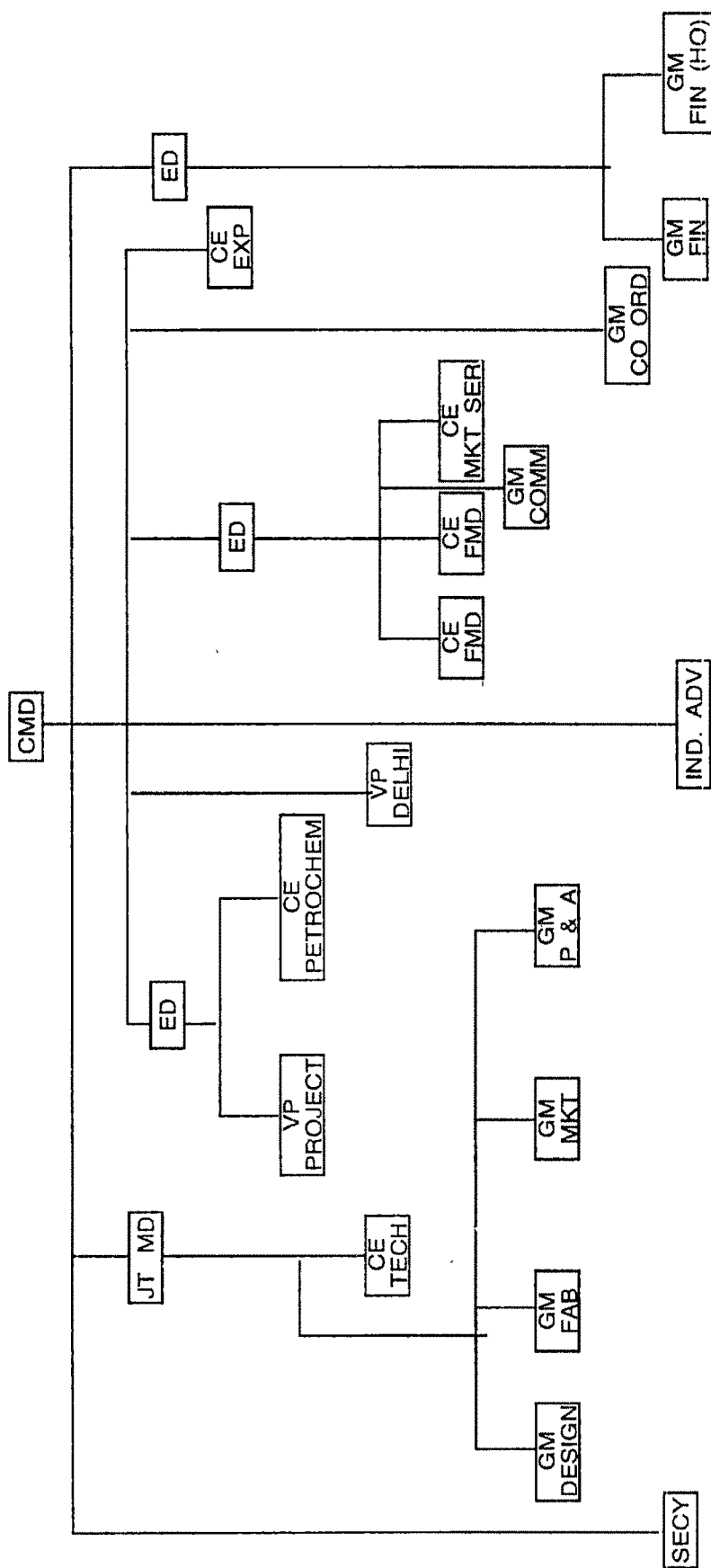
proposed near Jamnager will process petroleum crude to produce feed stock like kerosene, naphtha/NGL, and fuel oil for the down stream projects at Patalganga and Hazira.

The RIL has been quite aggressive and conscious about the quality of its products. To ensure this it has collaborated with world's eminent technology giants for its various products. The list of the foreign collaborators and their respective products is given in Appendix 5.6. Its plants are recognised as technologically most advanced in India. The Patalganga plant received the Prestigious Safety Award from British Safety Council for the year 1991, in recognition of its safety standards in man made fiber industry.

The major factors leading to the RIL's success on operation front are³¹:

- (i) An aggressive strategy for raising finance coupled with expansion programmes to minimise the tax liability culminating to lower cost of the expansion programme;
- (ii) an astute exploitation of loopholes in Government rules and regulations for its own advantage coupled with an unprecedented clout at all levels of Government policy-making that ensures that RIL's interests are safeguarded and even furthered;
- (iii) an innovative drive for technological modernization and vertical integration of its product-mix giving RIL an edge over all its competitors.

ORGANISATION CHART OF RELIANCE INDUSTRIES LTD.



SECY = SECRETARY
 GM = GENERAL MANAGER
 CE = CHIEF EXECUTIVE
 J.T. MD = JOINT MANAGING DIRECTOR
 P & A = PERSONNEL & ADMINISTRATION
 MKT = MARKETING
 EXP = EXPORT
 CO ORD = CO ORDINATION
 COMM = COMMERCIAL
 TECH = TECHNICAL
 FAB = FABRICATION
 FIN = FINANCE
 HO = HEAD OFFICE
 IND. ADV = INDUSTRIAL ADVISOR
 ED = EXECUTIVE DIRECTOR
 VP = VICE - PRESIDENT
 CMD = CHAIRMAN AND MANAGING DIRECTOR

Fig. 5.5

Organisation Structure

Fig. 5.5 depicts organisation chart of RIL. It has remained a closely managed company with only eleven members on its board. Of these two are nominee directors of FIs and three are outsiders (though M.L. Bhakta is inseparable from RIL and a key person in RIL's "inner think tank") and rest of the six members are closely related family members and friends (Refer Appendix 5.7 for the list of board of directors).

The major decisions are taken by closely held group of family members (known as "inner circle"). They are supported by highly qualified and experienced close allies and consultants (known as "inner think tank"). Then, the broad guidelines are issued over which the professionals have full freedom to act upon ³².

RIL is a typically family controlled company supported by highly qualified and experienced professionals. This is due to Dhirubhai's style of working and RIL's recruitment policies. Quite contrary to the popular concept of recruiting fresh personnel and train them in the company, RIL prefers highly experienced tested professionals for its projects. Once the concept is defined, RIL gives free hand to its professionals to carry out the projects.

Financial Strategy

Business Today (June, 7-21, 1992) started a cover story on Ambanis in their issue as:

"TAKE AMBITION. Add money. And the resulting acronym could well be Ambani. ...He used money - investors' money - to fuel his overpowering ambition to be numero uno in business. And he had used ambition itself as a lure for raising money from investors."

Since it went public in 1977, Ambanis have mobilised Rs.7970.12 crores; of which Rs.7507.64 crores were raised in Indian capital market and Rs.462.48 crores from international market in the form of Global Depository Receipts.

By the end of 1992-93, family of RIL shareholders was as large as 3.7 millions, largest in India. It is the confidence of these shareholders/investors which helped RIL to finance their mega plans. RIL have also served their shareholders by sharing their prosperity with them and designing the financial instruments mutually beneficial to the company and their shareholders. Ambani believes that prosperity, if shared, gets multiplied. (Refer Appendix 5.8 for capital structure of RIL since it went public).

Equity capital: The maiden public issue of RIL was made in November, 1977, to get listing on Bombay Stock Exchange. It was subscribed 7.19 times. It also issued an additional one lakh shares to 'Reliance Employees Welfare Association' (REWA). In 1979, rights issue at a premium of Rs.15 per share was made to comply with the listing conditions at Bombay Stock Exchange. In 1981, to finance its PFY project, rights worth of Rs.6 crores were issued at Rs.25 including Rs.15 premium per shares when RIL's share was quoted at Rs.98.

In 1987, one more rights issue was made for Rs.190 crores to

finance PTA, MEG, and HDPE projects. In addition to this, RIL has also given preference or rights to its shareholders in all its issues other than equity shares. It has also declared bonus in 1980 in the proportion of 3:5 by capitalising Rs.4.52 crores, and in 1983 in proportion of 3:5 by capitalising Rs.11.16 crores.

Preference Shares: In the year 1976-77, to finance the expansion phase I, the company issued 11 per cent 30,000 cumulative redeemable preference shares of Rs.100 each to the General Insurance Corporation. Further in the year 1982, with a view to augmenting the long-term resources, the company issued 5.5 lakh 13.5 per cent cumulative redeemable preference shares of Rs.100 each on right basis to its shareholders.

Cash Certificate: In 1985, it came out with cash certificate deposits of Rs.11.56 crores. The scheme was similar to the fixed deposit scheme with a difference that the repayment was scheduled to the next day following the date of maturity after three year. This provision made the cumulative returns on the certificate to the depositor a long-term capital gain which is taxed at a lower rate. It also helped the company to increase its profit as it has to charge the interest payable on such certificate only in the year of repayment and there is no annual charge.

Convertible Debentures: The company issued its I series of convertible debentures in 1979 when it was quite new and

untested instrument in Indian Capital market. This instrument for one thing, gave assured interest to its holder when project was at initial stage and allowed him to share prosperity through conversion once the project succeed in later years. On the other hand it relieved the company from annual charge and repayment of principal after the conversion. The company had issued partly convertible debentures of Rs.120 each of which 20% of this was to be converted into two equity shares at a premium of Rs.15 per shares; and remaining 80% non convertible portion was to be repaid in 4 annual instalment after ninth year of allotment. The issue of series I of Rs. 7 crores in 1979, to finance Phase II expansion, Series II of Rs.10.80 crores in 1980, to finance automatic looms and other machines, Series III of Rs.24 crores in 1981, to finance PFY project, Series IV of Rs.50 crores in 1982, to finance working capital needs and modernising the plant at Naroda.

In September 1984, in a brilliant and unconverntional move, RIL was able to convert a huge debt of Rs.73.5 crores (total amount outstanding after conversion on account of earlier four series of debentures) into a modest equity of Rs.10.3 crores in one stroke while it jacked up the reserves and surplus by Rs.63.2 crores. It offered to post-conversion debenture holders of I, II, III and IV series an exchange of 1.4 shares for every Rs.100 worth of debentures. In other words, the company exchanged Rs.10 shares for Rs.71 worth of debentures. The debenture-holders found the proposal attractive because they get a RIL share for Rs.71 while the

market price was Rs.115. In terms of cash outflow, RIL stood to gain. Given 30 per cent dividend rate, RIL will pay only Rs.3 crores as dividend whereas the annual interest burden on the debentures would have been Rs.9.65 crores. Moreover, the company now does not have to repay the instalments on debenture loan. The company also saved a colossal amount of paper-work. RIL till then had 1.2 million folios. Conversion of the I to IV series debentures into shares reduced the number of folios to less than half the original and reduced the administrative burden substantially.

In 1984, Series E of partly convertible debentures of Rs.80 crores were issued to finance expansion and modernisation of yarn and fabric divisions, at Naroda and Patalganga. In 1985, F - Series Non-convertible debentures of Rs.270 crores were issued to finance expansion of PFY capacity and commission of PTA and PAF projects. In 1986, G - Series fully convertible debentures of Rs.500 crores were issued to finance PTA, MEG and HDPE projects. In 1988, Rs.600 crores FCDs were issued by RPL to finance MEG, HDPE and PVC project. In 1989, L&T under the banner of Reliance raised Rs.820 crores FCDs to finance RIL's gas cracker project. In 1991, through H, J, and K series of partly and non-convertible debentures, RIL raised Rs.858.30 crores to finance its gas cracker project. In 1992, under the banner of Reliance, Reliance Polyethylene, Reliance Polypropylene, and Reliance Capital Finance Trust raised Rs.1,375 crores. Finally, in 1993, Reliance Petroleum Ltd. issued Triple option convertible debentures of Rs.60 each aggregating Rs.2,172 crores to finance its refinery project

near Jamnagar in Gujarat.

Global Depository Receipts: RIL is the first Indian company to issue Global Depository Receipts (GDRs). In 1992, it issued 92,00,000 GDRs at a price of US \$ 16.35 aggregating US \$ 150.42 million (Rs.462.48 crores); each GDR represents one Global Depository Share (GDS) and each GDS represents two underlying equity shares of Rs.10 each. This resulted in an increase in equity of Rs.18.40 crores and an addition to reserves by Rs.444.08 crores. They are listed at Luxembourg Stock Exchange and are also traded on Over The Counter (OTC) market in London.

Merger with RPL: The company has capitalised an opportunity created by the liberalization of Government policy and accompanying economic reforms by merging with Reliance Petrochemicals Ltd. (RPL). It was the ever largest merger in Indian corporate history in a record time of five months with effect from March, 1992. According to the company, the merger was aimed to enhance shareholder's value by realising significant synergies of both companies. The merger of RPL at 10:1 exchange ratio implied that Rs.593 crores equity of RPL added Rs.59 crores to equity and Rs.534 crores to reserves of RIL. This means that RIL got Rs.534 crores interest free. Not only that, in process, RIL increased its assets worth Rs.1750 crores which would add Rs.1100 crores cash flow in three years due to depreciation on RPL's assets and the losses of RPL is likely to help RIL to remain zero tax company for succeeding five years.

Financial Highlights

The scanning of financial statements for the last eight years from 1984-85 to 1991-92 is given in Appendix 5.9. The networth of the company during this period has increased nearly 8 times from Rs.246 crores to Rs.1943 crores at a compound annual rate of 30%, while, borrowings have also grown substantially i.e., 7 times from Rs.415 crores in 1984-85 to Rs.2936 crores in 1991-92, with compound annual rate of 26%. Therefore, debt equity ratio reflect declining trend from 1.12 in 1984-85 to 0.92 in 1991-92 which is quite lower than industrial average of 1.25. The total assets and Net block have also grown nearly 7 times during this period. Total assets from Rs.662 crores in 1984-85 to Rs.4880 crores in 1991-92 and Net block from Rs.426 crores to Rs.3338 crores showing respectively 28% and 30% annual growth rate.

The funds in working capital have been also increased manifold from meagre Rs.2 crores in 1984-85 to Rs.318 crores in 1991-92. The current ratio is stabilised in the range of 1 to 1.3. It is quite low when compared with the industrial average 2 to 3.

On operational side, turnover has increased nearly 4.75 times from Rs.622 crores in 1984-85 to Rs.2953 crores in 1991-92 with compound annual rate of 22%. Against this profit after tax has increased little more than 2.5 times during the same period from Rs.61 crores to Rs.163 crores, with 13% annual growth rate. The rate of change in profitability has been

quite volatile over the period. The ratio of PAT to sales has been consistently higher than industrial average. For 1991-92 it stood at 5.5% against the industrial average of 2.87%. Return on networth for 1991-92 was also little higher at 8.40% compared with 7.44% industrial average. The rate of dividend has remain higher than industrial average rate of dividend. For the last four years from 1988-89 to 1991-92 it has paid 20% dividend to its shareholders. The P/E ratio, market price and earnings per share have been quite volatile over a period of last eight years. For the year 1991-92, average market price, price-earning ratio and earnings per share was Rs.287, 61.7 and 5.74 respectively. Against this, book value per share has been consistently increasing from Rs.52 per share in 1983-84 to Rs.84 in 1991-92 with an annual growth rate of 7 percent. So far as serving of the shareholders is concerned, the rate of dividend has remained higher than industrial average rate of dividend. On an average it has paid nearly 35 percent dividend in the last eight years. For the last three years, it has paid stable dividend of 30 percent to its shareholders.

Creativity in preparation of Accounts

The accounting standards are prepared to harmonise the diverse accounting policies and practices prevalent in preparation of annual accounts which in turn ensure reflection of true and fair view of financial position of the firm. But in India, the accounting standards are only recommendatory and not statutory in nature. Therefore, Indian firms have been observed to have exploited these standards at

their advantages instead of following them in letter and spirit in preparing their annual accounts. The only deterrent is that the certified auditors are supposed to qualify the report if companies are not following the accounting standards which is more or less proved ineffective. RIL has been reportedly indulging in changing their accounting policies and practices to show favourable results in its annual report. Review is made here, to see how far it has adhered to the accounting standards issued by Accounting Standard Board.

The first standard "Disclosure of Accounting Policies" (AS-1) deals with disclosure of significant accounting policies followed in preparation and presentation of financial statements. The RIL has been found sufficiently disclosing its accounting policies and changes in accounting policies, its effect on the financial statement of respective year in its annual report to its shareholders (Refer Appendix 5.14 for such detailed disclosure since 1982).

Accounting standard-2 deals with valuation of inventories which was issued in 1981. Para 24 of this standard requires that inventories should be valued at lower of historical cost and net realisable value; para 29.3 requires that reusable waste should be valued at raw material cost less reprocessing cost and para 29.4 requires that non-reusable waste should be valued at its market value. RIL changed its accounting policies for valuation of inventory accounting according to this standard, in 1985. This resulted in reduction in profit

of Rs. 16.82 crores (Refer Appendix 5.15 for detailed disclosure).

Accounting standard-6 deals with accounting of depreciation and disclosure therewith. In 1982, RIL changed the mode of computation of depreciation in accordance with section 205 [2(b)] of the Companies Act, 1956 resulting in the increase of Rs. 16.34 crores in profit (Refer Appendix 5.14 for detailed disclosure).

Para 9.2 of Accounting Standard-10 dealing with accounting for fixed assets requires that interest on borrowed funds for construction or acquisition of fixed assets are to be capitalised for the period upto the completion of construction or acquisition of fixed assets are ready to be put to use. Till 1981, RIL used to treat the interest cost in accordance with the above standard, but it changed the method of accounting interest cost on fixed assets from 1982 to 1984. Again, in 1985 it changed its accounting policy retrospectively in accordance with the amendment in section 43 of Income Tax Act, 1956 vide Finance Bill, 1986 and in compliance with this standard. All these changes and their effects on financial statements of respective years (Refer Appendix 5.15 for detailed disclosure).

In compliance with Accounting Standard - 11, which deals with the effect of changes in foreign exchange rates RIL has changed its method of accounting of forex losses/gain on account of its borrowing in 1992 and 1993. This has resulted

in increase in the profit of the company by Rs. 4.11 crores and Rs. 28.40 crores in 1992 and 1993 respectively (Refer Appendix 5.14 for detailed disclosure).

Thus, RIL did indulge in changing its accounting policies more frequently to show the desired level of profitability but with due degree of disclosure.

Corporate rivalry

The RIL which otherwise would have been a low profile company has been brought into lime light by controversies raised in the press by Express group of newspapers under R.P. Goenka on account of inter-corporate rivalry of Ambanis vs Nusli Wadia. They have been old foes since they came into public prominence - Wadias, when he took over as Chairman of Bombay Dyeing and Ambanis, when the Reliance went public.

The rivalry which sparked off as trade rivalry has gone far beyond the market place. Recently, it has been intricately politicised and criminalised too³³. Being involved in the same industry, having manufacturing complexes in same industrial area, each one had used his political connections in the age of permit raj to disadvantage each other. A chronology of twists and turns of their bizarre corporate rivalry which allegedly took criminal and political overtones are given in Appendix 5.10.

The examples in context are, the non Congress Governments helped Wadias and restricted Ambani's business developments,

where as Congress Governments helped Ambanis and consequently caused disadvantage to Wadia. It is alleged that, harassment to Wadia through investigation of his citizenship issue, halting the crucial plant of Bombay Dyeing, and restricting the supply of scarce raw material for textile industry (including Bombay Dyeing) were at the behest of Ambani's political connections. On other hand, publication of series of anti-Ambani articles in press specially, at a time when Ambanis were coming out with an issue to raise finance from the public, allegation of smuggling of plants, and use of Government agencies to investigate the deals of Ambanis in Fairfax episode were at the behest of Wadia's political connections. And, finally a real or a frame up story of conspiracy to kill Wadia, again at a time when L&T, under the seige of Ambanis was about to come out with Rs.820 crores issue, added a criminal overtone to this rivalry. Reacting on this episode, Jaswant Singh, Member of Parliament, stated that

"...The main reason behind this development is that some people and some business houses consider that they own the State and the Government".³⁴

Not only that, it was reported that it was this feud caused a rift between Rajiv Gandhi and V.P.Singh in 1987 which ultimately led to latter's exit from the Government and caused sort of polarisation in the entire political system³⁵. As press reports had it, this rivalry had played a definite role in keeping Ambanis away from L&T and sufficiently apprehended the Government to take any open stand in this issue.

5.3. ROADS TO MARKET FOR CORPORATE CONTROL

This part attempts to unfold the causes which led the Ambanis to takeover the reins of L&T. It also gives an account of the underlying motivations which guided them unrelentlessly to consolidate their control over L&T.

5.3.1 Internal Problems

N.M.Desai, the then President and Managing Director of L&T was to retire in March, 1989. He had been with L&T since he was twenty two years old and had grown in L&T with its founder members. He had been occupying this position since 1978. It was reported that he kept the succession issue at abeyance all along even after getting reminders by insiders and institutional directors, as the top management had been riven by severe discord from 1985-86. Finally, when N.M.Desai superseded the senior executives to appoint his favorite as his successor, they were highly dissatisfied and started leaving L&T. The conflict for the leadership got complicated and brought out L&T leadership issue on corporate streets from its board room.

There were legal suits against N.M.Desai for the mismanagement of resources of the company and selling away precious assets (real Properties) of L&T at throw away prices to parties related to him. Reportedly, the Company Law Board had issued notice under section 408 of The Companies Act, 1956, "to prevent oppression" by board of directors of any member of the company and "to safeguard the interest of

the shareholders and the public". Though the Company Law Board did not find any substantial evidences to appoint the

Table 5.2 : Changing Patterns of Shareholding in L&T during the Takeover Attempts

SHAREHOLDERS	SHAREHOLDINGS AS ON			
	I 9/3/88	II 10/10/88	III 18/9/90	IV 1/8/91
FINANCIAL INSTITUTIONS	39.16	32.24	41.05	40.24
NATIONALIZED BANK & THEIR SUBSIDIARIES	0.81	7.75	-	0.40
CORPORATE BODIES	3.47	3.47	21.8	21.53
PUBLIC AND OTHERS	56.09	56.56	37.15	37.83
DIRECTORS	0.47			

Notes and sources: A. Business India, March, 9-16, 1988.

B. L&T Ltd. vs Harish Jagtiani, AIR, 1991, SC, 1420.

C. The Stock Exchange Official Directory, The Bombay Stock Exchange, Bombay.

D. The Economic Times, 21/09/91

1. This includes 6.45% stake which was later transferred to TILL.

2. It includes the investment by banks and its subsidiaries and the earlier 6.45% of L&T which was retransferred to FIs by TILL.

3. Includes 16.5% held by TILL.

4. Includes the stake of directors.

Government director but suggested that FIs should be more active and revamp the management, if necessary.

5.3.2. Ownership Pattern:

Besides these internal problems, the major cause that made L&T a candidate for takeover target was its ownership pattern of equity capital. The shareholding pattern during the various stages of takeover attempt is given in Table 5.2. There is conspicuous absence of any major shareholder having more than 2% equity stake in the company except FIs holding

substantial 39.97% equity stake. Thus, FIs held the key for control over L&T.

5.3.3. Government Interface:

In early 1988, The Companies (Amendment) Bill, 1988, was announced. This Bill proposed severe restrictions on the discretion of the management to refuse transfer of shares. It proposed to make it obligatory on the part of the management to intimate the refusal of transfer, within two months of delivery of application for transfer, to the transferee and the transferor. In order to save the L&T from raider, the management had carved out the stock option plan to make the employees of the company the largest shareholder with 10% equity stake. But the plan was turned down by Controller of Capital Issue (CCI)³⁶.

5.3.4. Unwanted Raider and White Knight

By early 1988, Chhabrias³⁷ had reportedly cornered 1.5% equity of L&T and were not far from taking over L&T successfully. This was reported to be not acceptable to N.M.Desai, as he had hardly weeded out the unwanted men in his company to be his successor. Besides, there was a flutter among majority of the senior executives in L&T. When it became inevitable that Chhabrias would sooner or later takeover the L&T, the press reports had it that N.M.Desai might have preferred some Gujarati to takeover L&T to a Sindhi. Thus, N.M.Desai might have invited Ambanis to save L&T. The Ambanis, on accepting the request, started taking positions in L&T and influenced FIs not to support

Chhabrias³⁸. Obviously, in a company, where FIs were the biggest shareholder and the management have very small equity stake along with no major private shareholder, the support of FIs became decisive in taking over a company.

5.3.5 White Knight turned Raider

The ownership pattern of equity capital of L&T played a decisive role in weeding out the Chhabrias and heralding the entry of Ambanis in L&T. On the strength of their known political clout, Ambanis believed that the target had been shot and started consolidating their control. This was the first major turning point in shaping the future course of events that were yet to unfold at L&T.

5.3.6. L&T - Reliance Alliance

Ambanis perceived that L&T being a blue chip, cash rich and highly under leveraged firm, it could be used as conduit to raise finance from the public which in turn could be diverted to finance (Reliance Petrochemicals Limited (RPL): On an average the debt equity ratio of L&T is 1:1. In the last five years, it has been consistently less than one hence, taking 2:1 as standard, it had at any time unused borrowing potential equal to its net worth.

For L&T, RIL meant a greater financial strength and risk taking capability. The undisputed political clout of Ambanis would mean much faster growth of L&T's core business i.e., heavy engineering. It was reported that despite its highly qualified and professional manpower, its growth had been

hampered on account of its inability to get the approval from the Government and to compete with much favoured public sector companies.

For Ambanis, control over L&T meant association with incomparably superior engineering skill and professional management. L&T was also critical for the development of Ambanis' petrochemical complex at Hazira, which otherwise would have been developed by foreign engineers costing very heavily to Reliance. L&T was also to serve for Ambanis as launching pad to venture into capital intensive or high technology area like electronics, fertilizer, construction, oil refinery, and turnkey contracting, both in India and abroad. To sum, according to Ambanis, "Reliance - L&T alliance is a lethal combination of enterprenureal and professional skills"³⁹.

5.3.7. Psychological Instincts

The above factors in consonance with some underlying subtle psychological instincts like the urge to grow, obsession to be the highest and ego (prestige) gave the major thrust to Ambanis to unrelentlessly stalk L&T to any extent and with any means whatsoever.

5.4. COMPETITION FOR CORPORATE CONTROL

This section narrates various twists and turns and related issues in L&T takeover attempts in two parts⁴⁰. Part one narrates the entry and the exit of Ambanis from L&T and

discusses the major issues regarding the route adopted by Ambanis to enter L&T; the role played by FIs in inducting and removing the Ambanis from L&T; and the inefficiencies of legal provisions to justify their obsolescence and indolence. Part two narrates the post exit happenings and determined but unsuccessful attempt by Ambanis to regain control over L&T through unprecedented historical proxy collection drive and discusses the indecisive stand of FIs on this case besides pointing out the debilities of legal provisions encountered by parties involved in the takeover. The chronology of major events of this battle is given in Appendix 5.11.

5.4.1. Part I: Entry and Exit of Ambanis from L&T

The drama started with the incorporation of Bank of Baroda Financial Services Ltd. ("BoB Fiscal"), a wholly owned subsidiary of Bank of Baroda. Premjit Singh, the then Chairman of Bank of Baroda and his son Harjit Singh had strong business connections with Ambanis. The BoB Fiscal had purchased thirty nine lakhs shares (6.5% of equity capital) of L&T from FIs in two separate transactions; one on October 11,1988, for thirty three lakhs shares and another on January 6,1991, for six lakhs shares. On the day (October 10,1988) when L&T registered the shares so transferred in the name of BoB Fiscal, Mukesh Ambani and B.L.Bhakta, nominees of Ambanis, joined the L&T's board. Meanwhile, Reliance Petrochemicals Ltd. launched its mega issue of Rs.594 crores. BoB Fiscal then transferred the shares of L&T purchased from FIs to Trishna Investment and Leasing Ltd. (hereinafter referred to as "TILL"), a wholly owned subsidiary of RIL at a

consideration of Rs.30 crores (@ Rs.76.92 per share). The jolt was yet to come. Shortly after that the L&T board had Anil Ambani as additional director and D.H.Ambani as its chairman. Thus, L&T officially became a part of the House of Ambanis.

Ambanis started milking the cash cow (L&T); they redefined the financial strategy, to finance their plans with the available and potential resources of L&T. The board under the chairmanship of Ambanis sanctioned investment of Rs.76 crores in RIL, mega issue of L&T of Rs.820 crores in which Ambanis gave preferential allotment to shareholders of RIL and RPL. More than three forth (77.4%,precisely) of the mega issue was to finance Ambanis projects through contracting turnkey projects including the arrangement of supplier's credit of Rs.510 crores.

Meanwhile, two shareholders (Harish Jagtiani and Shamit Majumdar) filed a writ petition in Bombay High Court challenging the entry of Ambanis in L&T and Rs.820 crores mega issue. The Bombay High Court dismissed their plea in its judgment on September 29,1989, and the petitioners preferred an appeal with the Supreme Court. During the hearings in Supreme Court, the Government was changed at the Parliament and V.P.Singh, known for his anti-Ambanis stand, became the Prime Minister. Ambanis initiated for compromise but it was not acceptable to petitioners. In a dramatic turn and as a "expression of goodwill" TILL retransferred the block of shares (39 lakhs shares of L&T) to FIs, incurring a loss of

Rs.10 crores; FIs called an extra ordinary general meeting ("EGM") to remove Ambanis from the board of L&T. These events reversed all the equations of the power game started by Ambanis and culminated in the resignation of D.H.Ambani from the board of L&T in "a gesture to observe corporate democracy".

During their tenure at L&T Ambanis played two decisive tactical moves with a view to furthering their efforts to regain control over L&T. Firstly, they appointed Reliance Consultancy Services (RCS) as Registrar of the shareholders and debentureholders of L&T. Secondly, they ceded a senior executive of RIL, as company secretary of L&T. In any takeover battle, the registrar of members and the company secretary of the target company play pivotal role in defending or facilitating the takeover of the target company.

With the removal of Ambanis, D.N.Ghosh, a former Chairman of State Bank of India, as a nominee of FIs, took over as Chairman of L&T. The board under the Chairmanship of D.N.Ghosh cancelled the supplier's credit to RPL, pruned the mega issue, and liquidated half of the L&T's investment in RIL at profit. Thus, in addition to looking after the wounded prey - L&T, he started reversing the decisions taken by Ambanis. But L&T was destined to suffer one more blow.

The National Front Government led By V.P.Singh could not stay for the mandated term owing to variety of reasons such

as the contest for leadership (as Devilal and Chandra Shekhar were also ambitious of becoming Prime Minister) and the indecisive stand on Babri-Masjid issue. The inter-ministerial conflict halting further liberalisation of industrial policy and aggravated nation's fiscal imbalance. Finally, acceptance of Mandal Commission report culminated in exit of National Front Government.

Chandra Shekhar with the tacit support of Congress (I) was invited to form the Government at the Parliament. The known motive of Congress(I) behind supporting Chandra Shekhar was to extend the political uncertainty till Rajiv Gandhi find an opportune time to strike back. The Ambanis were also waiting and preparing to strike a blow on their coveted prey - L&T. They succeeded partly as D.N.Ghosh resigned from L&T on instructions from top without disclosing any reasons (the extract of his resignation letter is given in Appendix 5.12). Meanwhile, the Supreme Court also upheld the mega issue of L&T floated by Ambanis without any modifications strengthened Ambanis for the next move. It was also widely believed that Congress (I) under leadership of Rajiv Gandhi would come to power in the then impending parliamentary elections. But L&T takeover case had still a long way to go. In a human bomb, Rajiv Gandhi was killed in an election campaign on 20th May, 1991. In the election, though Congress(I) though did not get the clear majority but emerged as a clear winner in the Parliament. P.V.Narasimha Rao was elected as leader of the party and sworn in as the Prime Minister. The Ambanis, meanwhile, went into hibernation to take respite. This was

akin to a lull before the storm.

5.4.2.Role of Market Participants

The events starting from back door entry and leading to reluctant exit of Ambanis from L&T are discussed above. The critical evaluation of strategies and tactics adopted by various market participants responsible for this episode is made as under.

Innovative route for acquisition of substantial shares

The Ambanis, through the instrumentality of FIs cornered 6.45% of equity stake in L&T in a so called "commercial transaction". Later on, with the approval of Rs. 820 crores mega issue of L&T with preferential allotment to shareholders of RIL/RPL, they succeeded in raising equity stake of RIL/RPL family (all the shareholders in RIL/RPL) in L&T to staggering 35.5% and simultaneously diluting the FIs's equity stake to merely 22.9%. This enabled Ambanis to "create a favoured lobby among shareholders, debentureholdders and employees to perpetuate their control over L&T". Dismissing the judgment of Bombay High Court and criticising the involvement of FIs, the Supreme Court in the case of L&T Ltd. vs Harish Jagtiani concluded that

" All these circumstances taken together clearly spell some doubt whether the transfer of such huge number of 39 lakhs shares by Public Financial Institutions was for public interest and was made on purely business principles (para. 23)".

Role of Financial Institutions

The role played by the FIs through their nominee directors is open to question. Firstly, why FIs did not raise any objection on or investigate into the cooption of two outside directors on the board on the day on which 7% equity stake of L&T was being transferred in one of the private deals to a subsidiary of nationalised bank? Did they know the ultimate buyer of 7% equity shares, in L&T sold by them to BoB Fiscal? If yes, then it implies that FIs were actively colluding in surreptitious transfer of reins of L&T. Besides, they were also involved in defeating the spirit and intention of Clause 40A and 40B of Listing Agreement. Were these acts in public interest ? If yes, possibly it would call for redefinition of "public interest" and scrapping of Clause 40A and 40B from Listing Agreement. If no, then penal actions have to be taken for the breach of trust. Alas, there is no law in India in this behalf!⁴¹

Secondly, what follows from above is that the holding of substantial equity stake in the private sector companies appears to be the antitheses of developmental role of FIs. On selective basis, there is always a case for having equity participation but it is not at all necessary for blue chip companies like L&T and that to an extent of 40%. The primary role of FIs is not to make enormous capital gain through equity participation but to act as catalyst in the development process. Therefore, they do not have to sit on their investment in prosperous companies in private sector for too long. This has led not only to the blockage of scarce

resources but also restricted the funds which otherwise could have been used for any other developmental purposes⁴².

Thirdly, the nominee director should ensure that tendencies of the companies towards diversion of funds to other companies of controlling group are curbed. Then, why did not nominees of FIs prevent Ambanis from passing resolutions for mega issue with preferential allotment, supplier's credit to RPL (Rs.510 crores), investment in shares of RIL (Rs.76 crores), while later on they unanimously voted against all these decisions. This was because of the change of the Government at the center. The FIs should not forget that they are on the board of private sector assisted companies on account of the investment of public money. Therefore, their actions in such companies should be guided by the cannons on "public interest" and not by the dictates of the central Government. The definition and scope of "public interest" do not necessarily change with the change in the central Government. Besides, it proves that the nominees are the arms of political control and their decisions are governed by political rather than economic considerations (Nevin,1961).

Fourthly, it is envisaged in a mixed economy that the intervention of the Government is required at times, during the transformation of economy when the market is not reasonably perfect to function efficiently. This could be through active but constructive participation in the market. Therefore, ideally, the role of FIs is to enforce correct market discipline and to promote corporate democracy. They

shattered the very concept of constructive intervention, by removing Ambanis from L&T when the latter had the right to control L&T under corporate democracy, and had inducted them when they were not holding even a single share of L&T in their own name. This is one of the cases, where the real owners - small shareholders at large across the country - are at the mercy of FIs acting either on instructions the Government at the center or in collusion with one of the major private shareholders. Thus, the essential role expected to be played by FIs on corporate boards is to liberate the board from the absolute domination of controlling group and not other way round.

Legal issues

The entry and exit of Ambanis in L&T has brought into light the inefficiencies of some of the legal provisions served their intent either by not observing or by avoiding them. This seems to have been possible because of their being loosely drafted, vulnerable to ambiguous interpretations and absence of deterrent penal provisions for non-observance.

Firstly, Ambanis successfully avoided compliance with Clause 40A and 40B of Listing Agreement which requires a person, taking over the control of the listed company, to make public offer to remaining shareholders of the company to buy their shares at negotiated price. The scope of this provision is too narrow. It is a sort of a nature of contract between stock exchange and a listed company without any statutory backing. Further, in the case of default, surprisingly, the

listed company is penalized instead of party taking over the company thereby prejudicing the interests of non-managerial shareholders (instead of protecting their interest). Nothing was done to Ambanis, in this case, for avoiding these provisions.

Secondly, section 163(2) of the Companies Act, 1956, obliged the company to allow the inspection and to make extracts from any register of members or debenture holders or any other person (with prescribed fees). In this case, Ambanis did not submit the list of shareholders to a member not less than LIC of India holding 18% stake in the company. This is the corporate right of a member conferred on by the legislation, which should be implemented strictly. The reason for the violation of this section may be the absence of sufficiently deterrent penal provisions for its violation. Therefore, to enforce this section in its true spirit some criminal penalties should be timely incorporated in this section.

Thirdly, the Supreme Court, while giving judgment in this case, made some meaningful clarifications on the act of cornering of shares. Disapproving the judgment of Calcutta High Court in Babulal Chokhani vs Western Theatres, Justice Kasliwal stated that " We cannot subscribe to the contention that there was nothing wrong or illegal" in the action of Reliance Group of cornering or surreptitious purchase of the shares of L&T through intermediaries. Clarifying further on the acquisition of shares by Ambanis, he continued

"...it is no doubt correct that any person or company is lawfully entitled to purchase shares of another company in open market, but if transaction is done surreptitiously with *mala fide* intention by making use of some public financial institutions as conduit in a clandestine manner, such deal or transaction would be contrary to public policy and illegal" (L&T vs Harish Jagtiani and others, AIR, 1991, Supreme Court, 1420, para 68,69).

Fourthly, it has been established during the hearing of this case in the Supreme Court that the funds used for the acquisition of shares of L&T

"...were provided by the Reliance Group from out of the money received by the issue of convertible debentures for Rs.594 crores to public and others".

It was a blatant violation of section 73(3) of the Companies Act, 1956, which regulates the parking and utilisation of application money from the public. The noncompliance of section 73(3)) imposes fine, on the company, and every officer of the company who is in default, which may extend to five thousand rupees. By no means, it could be considered deterrent enough to prevent diversion of crores of rupees in market for corporate control.

5.4.3. Part II: Post Exit Happenings and Proxy Drive

After a short respite, Ambanis again struck with a bang!! On the strength of shareholding of TILL, Ambanis requisitioned an EGM to appoint on the board of L&T (i) D.H.Ambani as Chairman, and (b) Mr., Mukesh Ambani as Vice-President.

P.V.Narasimha Rao was elected as the new Prime Minister of India. Reportedly, he did not want to interfere in the controversial issues like this, as the Government was more

worried to strengthen its own position in the Parliament to successfully pass the pending Finance Bill 1991, and other important legislations (out of 526 seats on which election was held, Congress (I) won 230 seats substantially less than the required majority to pass any Bill/resolution). It was also reported that the Government had also requested to postpone the scheduled EGM, till the said Bill was passed successfully in both the Houses. But by that time it was too late for Ambanis to back out. This time Ambanis made a move without political support. Possibly they believed that investor's community at large would prefer them on the board of L&T. The hectic canvassing for and against Ambanis charged the environment, to an extent never witnessed before in the Indian corporate world. The Indian Express, published series of anti Ambanis articles. Virtually, every concerned investor, whether shareholder of L&T or not, impatiently waited for the EGM scheduled on August 26, 1991.

But the writings on the wall were different. The meeting was started with an initial motion to appoint the Ambanis on the board, by representative of TILL, D.K.Bhandary. Before discussion could start on this motion, representative of LIC of India, B.R.Gupta moved a resolution for the adjournment of the meeting. No sooner this resolution was moved, A.S.Gupta, Chairman of the meeting, adjourned the meeting on getting the information from the Police that a bomb had been implanted in the meeting hall. Later on, it turned out to be a hoax. All the efforts of Ambanis for collecting the proxies temporarily went in vain. They claimed to have submitted

82,964 proxies representing 3,65,87,067 shares controlling 48.1% stake in L&T (including the holdings of TILL). Meanwhile, two shareholders (M.G.Jajoo and Shamit Majumdar) of L&T went to Bombay High Court to obtain stay against the holding of EGM on the basis of the following grounds :

- (a) the appointment of the Chairman is the prerogative of the board and taking the same to the general meeting is against Article 136F of the Articles of Association of the company;
- (b) the notice of EGM does not contain explanatory statement as required under section 173 of The Companies Act 1956; and
- (c) the Ambanis have forged the proxies.

They also sought permission to verify the proxies within 48 hours of the starting of adjourned meeting as permitted under section 176 of The Companies Act 1956. The FIs which sought adjournment of original meeting on account of verification of proxies neither care to raise a point nor help in the verification of the proxies. The Court refused to stay the adjourned meeting but restrained to move a resolution seeking appointment of Mukesh Ambani as Vice-President. In an unexpected move, the Ambanis withdrew the proposed resolutions to be passed at the adjourned EGM as soon as the meeting started its proceedings. Meanwhile, in a annual general meeting of L&T on September 20, 1991, a move to remove Reliance Consultancy Services (RCS) as registrar of the company miserably failed in which FIs abstained from voting⁴³. This exposes blatantly the invisible hand of corporate rivalry hindering the Ambanis from taking over the

L&T.

On an application filed by shri M. G. Jajoo, a shareolder of L&T, at Esplanade court alleging forgery and cheating in collection of proxies, the court directed the police to investigate the issue on finding the prima facie commission of cognizable offense. The fight for corporate control is still going on latently. The Ambanis licked their wounds. Unrelentlessly, in the subsequent month in the annual general Meeting of RPL, D.H.Ambani rehearsed, "Corporate democracy will be restored at L&T ".

5.4.4. Role of Market Participants

The strategies and tactics adopted by market participants in post-exit happening and re-emergence of Ambanis to takeover L&T were highly controversial. The hostility in this episode has led one to create "bomb hoax" and reported forgery. Major issues involved in this episode are discussed as under.

Role of Financial Institutions

Firstly, it is not clear that, if the Government does not want to interfere, then why it sought the adjournment of EGM of L&T? It was reported that the Government wanted to adjourn the meeting till the Finance Bill, 1991 get passed successfully in the Parliament. The minority Government of Congress (I) led by P.V.Narasimha Rao, feared that any stand taken by FIs on L&T issue would create difficulties in passing the crucial Finance Bill, 1991. To their pleasure, before they could adjourn the meeting, the "bomb" hoax

adjourned the meeting saving their face in the public. It indicated an active play of invisible hand in the affairs of L&T. The culmination of intricate association of corporate houses with politicians is mind boggling. The issue unfolds the rot in the system which should be cured before it takes its toll.

Secondly, why the LIC which requested to adjourn the EGM to verify the proxies at original meeting did not raise any objection at the time of the adjourned meeting? Was it because of the reason that the Parliament had passed the Finance Bill, 1991, successfully? (The Finance Bill, 1991, was successfully passed just twenty four hours before the adjourned meeting, on September 15, 1991).

Thirdly, the two shareholders of L&T could take the issue of proxy drive to the Court, but what about those small shareholders/investors who neither have sufficient power and resources to object nor have any detailed information about the irregularities in the management of the company absolved by the board of Directors. It is, in these circumstances, nominees directors of FIs are expected to guard the interests of shareholders and public at large.

Legal issues

Firstly, the proxy contest in this case, exploded the inadequacies of the legal provisions under section 176 of the Companies Act, 1956, governing the proxy machinery in general and verification of the proxies collected by the contending

parties in particular. Section 176 does not regulate the mode of and price for collecting proxies and therefore, bidders have been observed to have collected through fair and foul means. Since collection of proxies is a cheaper way of collecting votes than to purchase shares from the open market, the collecting parties are ready to pay exorbitantly high premium on getting the proxies endorsed in their favour and to pay lucrative commission to agents collecting proxies on their behalf. Besides, in this case bidder was alleged to have forged the proxies and was also challenged in the Bombay High Court; an unprecedented issue in Indian corporate history. This issue was cleverly settled and "killed" by the Ambanis by withdrawing the proposed resolution at the adjourned meeting. Further, sub-section (7) of section 176 entitle the member to inspect the proxies lodged, during the business hours of the company from "the period beginning twenty four hours before the time fixed for the commencement of the meeting and ending with the conclusion of the meeting". This is impracticably a short time to inspect and verify the proxies when they are collected in large number as happened in this case. Besides, there is no legal machinery which can help the shareholders who want to inspect and verify the proxies. The two shareholders who applied for verification of proxies in this case, were thrown in the midst of 82,964 proxies. In a changed corporate culture the legal provisions should also be changed to have their meaningful existence.

Secondly, in another unprecedented issue in the annals of Indian corporate history, Ram Jethamlani, the Counsel for the petitioner, questioned the supremacy of general body of shareholders over the board of directors appointed by the former. It was argued that it is the power and prerogative of board of directors to appoint the managing director under Article 136F of Article of Association of the L&T and therefore, his appointment by the general body of shareholders is invalid. It was counter argued by R.Dada, the Counsel for L&T, stating that such power does rest with the shareholders to appoint managing director relying on sections 2(26) and 269 of the Companies Act, 1956. J.J.Bhatt, the Counsel for TILL, supporting R.Dada stated that though the primary power of appointment of managing director rest with the board, but if the board is unwilling or unable to exercise it, then by default, the residuary power comes to the general body of shareholders. The issue is still unresolved. In this case, the Court passed an *ad-interim* injunction order restraining the appointment of Mukesh Ambani in the pending adjourned meeting.

Thirdly, this case also witnessed one of the common weaknesses of Indian public limited companies of not disclosing or inadequate disclosure of the material information on proposed special resolution. It is mandatory under section 173(2) of the Companies Act, 1956. The explanatory statement annexed with the notice of the meeting called by TILL did not disclose the fact that both the directors viz., D.H.Ambani and Mukesh Ambani had resigned

from the board of the company earlier in 1989.

The competition for corporate control is going on in L&T, atleast latently. The interested parties are fighting for their own interests either in cash or in kind. Nobody cares for the tiny shareholder who has the right on the paper but does not have the might to enforce the right. He has to contend himself with small returns left out when major portion of the cake is eaten away by the predators. The protection of their interests is highly dependent upon the maturity of the stock market to enforce the transparency of the operations and efficiency of the market to process the given information.

5.5 SUMMARY AND CONCLUSION

The implications follow from the concentrated introspection into the subtleties of the successful and the unsuccessful attempt to takeover L&T by the Ambanis, are as under:

- (i) Legal provisions are neither sufficient nor adequate and ambiguous too, to enforce corporate democracy and transparency in corporate takeover transactions. The penal provisions are not deterrent enough to warrant their observance in letter and spirit.
- (ii) The decisions of the public financial institutions as a major shareholder related to transfer of corporate control have found erratic, and it has also been observed that they had no relation, whatsoever with the interest of the 'public', company and its

shareholders'.

- (iii) Corporate rivalries along with close nexus between politicians and corporate leaders are observed to have frustrated the market forces.
- (iv) In contrast to the accepted belief, the efficient performance, having good track record or the profitability even above industry average do not immune the company from takeover. In fact, in the present case study, precisely for these factors the bidder intended to takeover the target. The shareholding pattern and the succession problem are also observed to have led the L&T to market for corporate control.
- (v) The corporate ownership has to be analysed in a greater depth to find out some meaningful solution to retain and encourage private investment in more productive areas. If needed, the Constitution should be suitably amended. The law should be able to pinpoint the final responsibility of such complete volt face, which resulted into wastage of crores of rupees in the form of man-hours lost in unproductive uses.

To sum up, the case study exposes certain unresolved and disquieting issues regarding, the role of State or instrumentality of State when it ventures into corporate world; the indolence and ineffectiveness of the legal provisions to regulate the developments in market for corporate control; the inseparable alignment of business and politics which leaves the market forces useless and silent

spectator of blatant corporate-political conspiracy. The twists and turns of this case made the corporate democracy a subordinate to the Government bureaucracy led by political forces of highest level.

Notes and References

1. L&T is highly diversified engineering company managed by highly qualified and experienced professional. It enjoys blue-chip status among investors community.

2. The House of Ambanis, controlled by Dhirubhai Ambani and his family is one of the fastest grown Industrial Houses of Indian corporate sector in post-independent era. Within less than two decades of its existence it has the widest investors base in the country through its flagship company Reliance Industries Ltd.; the latter is also ranked biggest private sector company on many fronts like, sales, assets, net worth, profits, and dividend payout. The emergence of Ambanis in detail is given Appendix 5.5.)

3. Section 4A of the Companies Act, 1956, recognised following as financial institutions.

(1) Each of the financial institutions specified in this sub-section shall be regarded, for the purposes of this Act, as a public financial institution, namely:-

- (i) the Investment Credit and Investment Corporation of India Limited, a company formed and registered under the Indian Companies Act, 1913 (7 of 1913);
- (ii) the Industrial Finance Corporation of India, established under section of the Industrial Finance Corporation Act, 1948, (16 of 1948);
- (iii) the Industrial Development Bank of India, established under section 3 of the Industrial Bank of India Act, 1964, (18 of 1964);
- (iv) the Life Insurance Corporation of India, established under section 3 of Life Insurance Corporation of India Act, 1956 (31 of 1956);
- (v) the Unit Trust of India Act, 1963 established under section 3 of the Unit Trust of India Act, 1963 (52 of 1963).

(2) subject to the provisions of sub-section (1), the Central Government may, by notification in the Official Gazette, specify such other institutions as it may think fit to be a public financial institution;

Provided that no institution shall be so specified unless-

- (i) it has been established or constituted by or under any Central Act or
- (ii) not less than fifty-one percent of the paid up share capital of such institution is held or controlled by the Central Government.

4. Jensen, M.C. and Ruback, R.S., (1983), The Market for Corporate Control, p.6.

5. Hazari, R.H., The structure of corporate private sector: A study of concentration, ownership and control, p.329.

6. Weinberg, M.A., (1971), Weinberg on Takeover and Merger, pp.14-15. He distinguishes the impersonal shareholder from normal shareholder as the prime interest of the impersonal investor/shareholder is capital profit, rather than the income his investment produces. He may not be directly

interested in the affairs of the company.

7. The Indian corporate history is full of instances of family splits which led consequently to transfer of corporate control, for example, Modis, Birlas, Mafatlals, Bangurs etc.

8. In public tender offer, the offer price has been quite frequently more than fifty percent of the previous year's average share price, for example, public tender offers of John Fowler Ltd., Surat Electricity Ltd., Wendt India Ltd. etc. It is also reported that secret buying in Surat Electricity Ltd. was being carried out at price three times higher than its previous year's average share price.

9. It was reported that in the proxy contest of Gammon India Ltd., twenty five rupees per proxy of each share was paid to shareholders of Gammon India Ltd..(Illustrated Weekly, February 19,1989). The Ambanis, in this case, have also reported to have paid Rs.5 per call to their agents for proxy collection (The Economic Times, 20-8-91).

10. To quote such a few provisions: section 81, 108, 108A to 108H, 111, 163, 169, 176, 187, 187A to 187D, 393 to 395, 397 to 409 of The Companies Act, 1956; section 22A of Securities Regulations Contracts Act,1956: section 19,26, and 29 of Foreign Exchange Regulation Act, 1973; Chapter III, part A covering section 20 to 26 of Monopolies Restrictions and Trade Practices Act, 1969 (This part has been omitted by MRTP (Amendment) Act,1991, with effect from 27-9-1991); section 2(IA), 72A, 79 of Income Tax Act,1961; section 11(h) of Securities & Exchange Board of India Act, 1992, and Clause 40A and 40B of Listing Agreement and recently recommended Takeover Code.

11. According to study carried out by Center for Monitoring Indian Economy (CMIE) of 1290 listed companies, the Government/the Government sponsored institutions hold on an average thirty two percent ownership of these companies through equity shareholdings (11.13, Basic Statistics:All India, CMIE, August, 1993).

12. The Central Banking Committee, way back in 1931, recognised the "gaps" in capital market and recommended that special institutions have had to be created with the support of the Government to fill the gap in the structure of lending institutions. (para 7.14, Report on Industrial Licensing Policy Committee (Dutt committee), 1969).

13. Gupta, L.C.,(1969), Changing structure of Industrial Finance in India: The impact of Institutional Finance, p.15.

14. Dutt committee discusses at length, whether market purchases by LIC and UTI can be treated as assistance to firms in whose shares the investments are made. Normally, inspite of substantial equity holding, they do not interfere in internal management of the company except under special circumstances. Therefore, promoters would like them to hold substantial equity holdings in the company, thereby, reducing

their effective equity participation. To an extent the funds saved on account of such reduced participation can be considered as an assistance by these institutions. Besides when promoters are in need of fund, they may find it useful to sell their partial stake in the firm to these institutions with an understanding that this will not have any adverse affect on control over the firm. Thus, the new investments made by these institutions may be taken, as at least to some extent assistance to the firms (para 7.66).

15. The report of High Powered Committee on Stock Exchange Reforms (G.S.Patel committee),(1985), Minister of Finance, Government of India, New Delhi.

16. Dutt committee, *op.cit*, (para 7.30).

17. Dutt Committee, *op.cit*, (para 7.25).

18. Gupta, L.C.,(1969), *op. cit.*, p.63.

19. Industrial Licensing Policy Committee (Dutt Committee), (1969), Ministry of Finance, Government of India, New Delhi.

20. Srivastava, U.K. and Oza,N.M., (1980), Stipulation and Exercise of Convertibility Options, p.8.

21. Gupta, L.C., (1989), Corporate Boards and Nominee Directors, p.29.

22. Srivastava and et al., *op cit*, p.93.

23. Guidelines issued by Industrial Development Bank of India in 1986.

24. Gupta, L.C., (1989), *op. cit.*, p.30.

25. Life Insurance Corporation of India, Appellant, vs Escorts Ltd. and others, Respondents, All India Reporter, 1986, Supreme Court, 1370.

26. *ibid.*, p.8.

27. Larsen & Toubro Ltd.,Petitioner, vs Harish Jagtiani and others, Respondents, (para 10), All India Reporter, 1991, Supreme Court, 1420.

28. *ibid.*, para 33 and 34.

29. This consist of Reliance Industries Ltd. and erstwhile Reliance Petrochemicals Ltd.. The latter has been amalgamated with RIL with effect from March 1,1992, p.35.

30. Mohant, S.R., (1987), Reliance: An Industrial legend, Centre for Industrial and Economic Research, New Delhi.

31. Pandey, I.M., and Bhatt R.,(1989), The Sturdy Bubble, Cases in Financial Management, Tata-Mcgraw Hill Publication, New Delhi.

32. *op. cit.*, Mohant, S.R. (1987), p.125.
33. Business India, October 17-30, 1988, p.19.
34. *ibid.*, p.19.
35. The Economic Times, September 20, 1991.
36. The Office of Controller of Capital Issue was set up under Capital Issues (Control) Act, 1947. It was repealed by Capital Issue (Control) Repeal Ordinance, 1992.
37. After a lull in Indian market for corporate control due to aborted attempt by Swaraj Paul to takeover Escorts Ltd. in early 1980s, in later part of 1980s, Manu Chhabria created a flutter among Indian corporations by his corporate raiding spree. A Dubai based Non-Resident Indian, he is known for his aggressiveness and hostility in taking over target companies. The corporate battles of Shaw Wallace Ltd., Genelec Ltd., and Gammon India Ltd. marked the revival of hostile takeovers. His strategy for takeover was to buy large block of shares in the target company from Non-Resident shareholder abroad. The status of Non-Resident Indian gave him an additional advantage by exempting him from any investigation from Reserve Bank of India of source of consideration paid. By 1992, his corporate empire consisted of Shaw Wallace Ltd., Dunlop India Ltd., Mather and Platt Ltd., Hind-Dorr Oliver Ltd. (profit making companies) on one side, and Gordon Woodroffe Ltd., Falcon Tyres Ltd., Genelec Ltd., Orson Ltd., Nihon Electronics Ltd., Calcutta Chemicals Ltd. (loss making companies) on other.
38. Reports had it that Chhabrias got in tussle with Ambanis when he picked up 1.5% stake in L&T in which latter was also interested. In a retaliatory move, Ambanis went ahead and cornered shares of Dunlop India from the market through erstwhile BoB Fiscal. The two of them have reportedly sold off their respective stakes in each other's companies.
39. Business India, *op. cit.*, p.22.
40. The information under this section have been collected from various secondary sources like, The Economic Times, Financial Express, Business India, Economic and Political Weekly, judgements of the Supreme Court in case of L&T mega issue.
41. In case of LIC of India vs Escorts Ltd., the Supreme Court held that when FIs assume the status of ordinary shareholder in corporate world, they cannot be asked to give reasons for initiating the change in the management of the company.
42. Jayapandian, S., (1980), convertibility Clause and investment climate, p.39.

43. At the annual general meeting of L&T on September 20, 1991, the resolution to remove Reliance Consultancy Services (RCS) as registrar of the members and debenture holders of the L&T could not be carried out by show of hands at initial stage, and therefore a poll on the resolution was demanded. The result of the poll indicated that only 1,01,756 votes (only 0.24%) were cast in favour of removing the RCS against 4,16,77,702 votes cast in favour of retaining the RCS. The FIs abstained from voting. This amply proved that legal suits and anti-Ambanis campaign in media were sponsored and outcome of corporate rivalry.