

Legal Framework For Mergers and Acquisitions in India

* Dr. K. Srinivas

INTRODUCTION

Companies Come and Go, Chief Executives Rise and Fall, Industry Sectors Wax and Wane, but an outstanding feature of the past decade has been the rise of business combinations, which may take forms of mergers, acquisitions, amalgamations and takeovers, which are the important features of corporate structural changes. Business restructuring is often a one-time exercise, but has a lasting and telling impact not only on the business directly concerned, but also on the other connected agencies. The professionals have their tasks well cut out in this regard. The important legal and regulatory provisions for mergers and acquisitions are discussed in this paper. The Companies Act, 1956 has provided for a set of provisions specially dealing with amalgamation of companies to facilitate the transactions. The statutory provisions relating to M&As are contained under sections 390 to 396A of the Companies Act, 1956.

MERGER

A merger is said to occur when two or more companies combine into one company. One or more companies may merge with an existing company or they may merge to form a new company. In a merger, there is complete amalgamation of the assets and liabilities as well as shareholders' interests and business of the merging companies.

ACQUISITION

The term acquisition refers to acquiring of effective working control by one company over another. The control may be acquired either through purchase of majority of shares carrying voting rights exercisable at a general meeting, or controlling the composition of the Board of Directors of the other company.

OBJECTIVES

This paper is aimed at the following objectives:

1. To analyse the methods of Amalgamation, Merger or Amalgamation under Sections 391 to 394 of the Companies Act, 1956 and to analyze the procedure of amalgamation of companies by Central Government and to analyze the mergers in India in general.
2. To analyze the impact of Indian Competition Law on Mergers.

WAYS OF AMALGAMATION

Companies are amalgamated by any one of the following ways:

- **By the order of High Court:** Under Section 394 of the Companies Act, the High Court may sanction a scheme of amalgamation proposed by two or more companies after it has been approved by a meeting of the members of the company convened under the orders of the court with majority in number of shareholders holding more than 75 per cent of the shares who vote at the meeting.
- **By the Purchase of Shares:** Under Section 395 of the Companies Act, 1956, the undertaking of one company can be taken over by another company by the purchase of shares.
- **By Public Interest:** Under Section 396 of the companies Act, 1956, where the Central Government is satisfied that an amalgamation of two or more companies is essential in the public interest, then the government may, by an order notified in the Official Gazette, provide for the amalgamation of those companies into a single company.
- **Under Section 494:** Amalgamation of two companies is also possible under Section 494 of the Companies Act, where the liquidator of a company transfers its assets and liabilities to another company.
- **Under Revival and Rehabilitation :** The Board for Financial and Industrial Reconstruction (BIFR) can, in exceptional cases, order amalgamation for the revival and rehabilitation of a sick industrial company under the provisions of Sick Industrial Companies (Special Provisions) Act, 1985.
- **Under Sections 391-394 of the Companies Act, 1956:** Merger or amalgamation under a scheme of arrangements as provided under Sections 391-394 of the Act is the most convenient and most common method of obtaining a complete merger or amalgamation between the companies. The companies are required to obtain following approvals in respect of the scheme of amalgamation:
 - Approval of Board of Directors, Approval of Stock Exchanges, Approval of Shareholders/Creditors, Approval of Financial Institutions, Approval from the Land Holders, Approval of the High Court, Approval of RBI and Combinations under the Competition Act, 2002.

* Principal and Associate Professor, KGR Institute of Technology and Management, Rampally Keesara, Ranga Reddy - 501301, Andhra Pradesh
Email: ramatamsrinivas@gmail.com

PROCEDURAL REQUIREMENTS

While the statutory provisions relating to amalgamation of companies are contained in sections 390 to 396A of the Companies Act, 1956, the procedural aspects are covered by Rules 67 to 87 of the Companies (Court) Rules, 1959. The procedural aspects of mergers and amalgamations are:

Memorandum of Association

It has to be ensured that the objects of the Memorandum of Association of the transferee company cover the objects of the Transferor Company or companies; if it does not contain these, it will be necessary to follow the passing of a special resolution at an Extraordinary General Meeting convened for this purpose.

Convening a Board Meeting

A Board Meeting is to be convened and held to consider and approve in principle, the amalgamation and appoint an expert for valuation of shares to determine the share exchange ratio.

Valuation Report

An expert is requested to prepare a Valuation Report and the swap ratio for consideration by the Boards of both the transferor and transferee companies.

Scheme of Amalgamation

Companies which are to be amalgamated should prepare a scheme of amalgamation in consultation with the companies' auditors, legal advisers and Practicing Company Secretary. The scheme should be describing briefly the nature of assets and should also mention that rights and liabilities of the transferor company from the effective date will become the rights and liabilities of the Transferee Company.

Board Meeting

It would be necessary to convene a Board Meeting of both the transferor and transferee companies for approving the Scheme of Amalgamation, at least two days before the Board Meeting is proposed to be held for the purpose of approving the amalgamation.

Application to the High Court

An application seeking directions to call, hold and conduct meeting(s) is to be made to the High Court(s) in the manner prescribed under Companies (Court) Rules [Rule 67]. However, in small closely held companies, all the shareholders and creditors of the company give an individual "No Objection" to the Scheme of Amalgamation. The High Court then gives directions relating to the time, date and venue of the meeting of the equity shareholders of both the transferor and transferee companies and appoints a Chairman to conduct the meetings.

Sending of Notices etc.

Notices, Explanatory Statements and Proxy are required to be printed and dispatched to the shareholders after giving statutory notice required for the purpose, namely, 21 clear days of service of documents as required under the Companies Act, 1956.

Principles Governing the Explanatory Statement

The explanatory statement required under Section 393 is different from the one required under Section 173. The former does not ordain disclosure of all material facts. It should state the share exchange ratio but need not give details of calculation thereof, nor is it necessary to circulate the valuation report to shareholders.

General Meeting

At the General Meeting convened by the High Court, a resolution will be passed approving the Scheme of Amalgamation with any such modifications as may be proposed and agreed to at the meeting.

Reporting the Results

The Chairman of the meeting will submit a report of the meeting indicating the results to the concerned High Court in Form 39 of the Court Rules within 7 days of the conclusion of the meeting or such other time as fixed by the Court.

Approval by the Court

Court will fix a date of the hearing and the notice of the hearing shall be advertised in the same newspapers in which the notice of the meeting was advertised or in such other papers as the Court may direct not less than 10 days before the date fixed for hearing. The Court, after hearing all concerned, will pass an Order in Form 42 of the Court Rules approving the Scheme of Amalgamation.

AMALGAMATION OF COMPANIES BY THE CENTRAL GOVERNMENT

Exercise Power Under Section 396

The power under section 396 should be exercised by the Central Government only where the Government is satisfied that it is essential in the public interest that two or more companies should amalgamate. If the Government is so satisfied, it may pass an order providing for the amalgamation of those companies into a single company.

INTERESTS AND RIGHTS OF MEMBERS AND CREDITORS

Every member or creditor (including a debenture holder) of each of the companies before the amalgamation shall have, as nearly as may be, the same interest in or rights against the company resulting from the amalgamation as he had in the company of which he was originally a member or creditor [Section 396(3)].

PROCEDURE FOR SECURING APPROVAL OF THE CENTRAL GOVERNMENT

Section 396 does not expressly provide for an application to be made to the Central Government for an order for amalgamation. Any two companies wishing to amalgamate may submit a proposal to the Government for an order for amalgamation, the Boards of Directors of the two companies should pass a resolution for: Approving a scheme of Amalgamation; Authorizing a Director, Company Secretary or other officer to make an application to the Ministry of Company Affairs seeking an order for amalgamation. After the Boards of the two companies have passed resolutions, the Scheme of Amalgamation should be submitted to the Secretary, Ministry of Company Affairs, Government of India, New Delhi.

MERGERS IN INDIA

There are number of authorities and persons involved as required by the statute and specialized nature of activity to be carried out. High Court of the State where Registered Offices of Companies involved in merger is situated, the Government includes- Registrar of Companies, Official Liquidators, and Regional Director - Company Law Board, Central Government, and Authorities under respective statutes whose permission /approval is required in the course of merger, professionals covers- Chartered Accountants, Company Secretaries, Merchant Banker, Advocates, Counselors, and Venture Capitalists and the provisions of Companies Act dealing with mergers, acquisitions, takeovers and buyback are covered here. Relevant provisions are contained in Sec. 390 to Sec.396A of Chapter V of The Companies Act, 1956. Some other provisions having a bearing on Mergers and Acquisitions are also dealt with.

Table-1
Provisions Contained Under Section 390 to 396A

Sec-390(a)	‘Company’ defined
Sec-390(b)	‘Arrangement’ defined
Sec-390	Powers of a company to compromise or make arrangements with creditors and members.
Sec-392	Powers of the high court to enforce compromises and arrangements.
Sec-393	Intimation as to compromise or arrangements with creditors and members including the effect of the scheme explained.
Sec-394	Provisions for facilitating reconstruction and amalgamation. Approvals of the court, members etc.
Sec-394A	Notices to be given to the Central Government of every application under Sec-391 or 394. Representations, if any, to be made to the Government before passing any order under any of these sections.
Sec-395	Power and duties of a company to acquire shares of the shareholders dissenting from the scheme or contract approved by majority.
Sec-396	Power of the Central Government to provide for amalgamation in Public Interest.
Sec-396A	Preservation of books and papers of the amalgamated companies.
OTHER RELEVANT PROVISIONS	
Sec-108 to Sec-108I	Provisions relating to takeover of the company.
Sec-17	Alteration of Memorandum of Association.
Sec-319	Loss of office in the process of amalgamation
Sec-42	Membership of holding company.
Sec-77A,77AA & 77B	Provisions relating to Buyback of shares.
GOI Notification	Guidelines for buyback of Non-listed companies.
Sec-372	Provisions relating to investment in other companies.

Source: [www. Mergersindia.com](http://www.Mergersindia.com)

SEBI

The Securities and Exchange Board of India is the Controlling Authority for all matters concerning Stock Markets, Mutual Funds, Foreign Institutional Investors and other persons connected to securities, shares, mutual funds etc. SEBI, being a stock market watchdog has from time-to-time issued guidelines for different activities. SEBI Guidelines are SEBI (Buyback of Securities) Regulations, 1998, buy - back from existing shareholders, odd - lot buy - back of shares, offer procedure, escrow account, payment to shareholders and extinguishment of certificates.

SEBI TAKEOVER CODE

The term ‘Takeover’ has not been defined under the said Regulations, the term basically envisages the concept of an acquirer taking over the control or management of the target company. When an acquirer acquires substantial quantity of

shares or voting rights of the target company, it results in the substantial acquisition of Shares. A Public announcement is generally an announcement given in the newspapers by the acquirer, primarily to disclose his intention to acquire a minimum of 20% of the voting capital of the target company from the existing shareholders by means of an open offer. The filing of the draft offer document is a joint responsibility of both the Acquirer as well as the Merchant Banker. The acquirer is obligated to offer a minimum offer price as is required to be paid by him to all those shareholders whose shares are accepted under the offer, within 30 days from the closure of offer. The offer price shall be the highest of the negotiated price under the agreement, which triggered the open offer; price paid by the acquirer or PAC with him for acquisition of any, including by way of public rights / preferential issue during the 26 - week period prior to the date of the PA; and average of weekly high & low of the closing prices of shares as quoted on the stock exchanges, where shares of target company are most frequently traded during 26 weeks prior to the date of the Public Announcement.

SICK INDUSTRIAL COMPANIES (SPECIAL PROVISIONS) ACT, 1985

The mergers taking place are in a nature where loss-making companies are acquired by profit making ones. Once a company is declared “sick”, restructuring of the company has to be carried out as per the provisions and procedure laid down by SICA. These provisions will apply only in the cases of manufacturing companies where the company is atleast 5-year-old and when the net worth of these companies is fully wiped out. Provisions of Sec- 18(2) provides for various measures for revival of sick companies like financial reconstruction, amalgamation, change in or takeover of management, sale or lease of part or whole of industrial undertaking and also obligations of the transferee healthy company. Reverse merger is also permitted under the provisions of Sec- 18.

FEMA

The Foreign Exchange Management Act, 1999 was enacted to replace FERA, 1973 and made applicable from 1st June 2000. FEMA describes procedural aspects relating to foreign transactions and dealings and covers the issue and transfer of shares relating to amalgamation and other restructuring procedures. Issue and acquisition of shares after merger or demerger or amalgamation of Indian companies are pre-merger and post merger. Buy back of shares held by a person resident outside India will require the prior permission of the Reserve Bank of India. Application has to be made to the Reserve Bank in Form TS1 while considering the grant of permission.

IMPACT OF INDIAN COMPETITION LAW ON MERGERS

One of the basic objectives of the Competition Act, 2002 is to prevent practices that have adverse effect on competition. The Act prohibits creation of enterprises through acquisition or other structural combinations which may produce anti-competitive effects. The Section-5 definition of combination includes acquisition merger or amalgamation. Section 6(1) explicitly prohibits the combination which cause or are likely to cause an appreciable adverse impact on competition within the relevant markets in India. Exemptions are- Provision of Section-6(1) is not applicable to public financial institutions, foreign institutional investors, banks or venture capital funds. However, it is necessary to inform the Competition Commission of India within seven days from the date of acquisition.

CONCLUSION

Legal framework for mergers and acquisitions in India covers the ways of amalgamation that are : Sections 391-394 of the Companies Act 1956, amalgamation of companies by the central government, authorities involved M&As, SEBI norms, Sick Industrial Companies Act, 1985, FEMA, and Impact of Indian Competition Law on mergers. This paper would prove to be useful for understanding the legal procedure for mergers and acquisitions in India.

BIBLIOGRAPHY

- Growlery “The Merger Game Starts with Deception” Challenge, Sept-October 1986.
- Ranjana Kumar “Organization Turnaround of the Indian Bank” ASCI Journal of Management, 2006.pp18-26.
- M. K. Michael “Mergers & Acquisitions the Law of Mergers-II” The Chartered Accountant, December 1999.pp31-36.
- Anil. K. Sharma “Regulatory and Statutory Mechanism for Mergers and Acquisitions in India” International Journal of Management Sciences, December, 2005. Pp26-45.
- Helder Valente “Financial Strategies in Mergers and Acquisitions (M&A): The Case of Regulated Firms” CETE, May, 2003.
- Nimesh Shab “SICA A Takeover Guide” The Chartered Accountant, April 2000. Pp52-56.
- M.T. Raju and Deepthi “Market for Corporate Control and Takeover Regulations: Trends and Analysis” SEBI Working Paper No: 10, September, 2004.
- Vamsi Krishna “Mergers and Acquisitions Corporate Consolidation” The Chartered Accountant, May 1999. P 20-24.
- H S Chandhoke & Abdullah Hussain “Mergers Qua Competition Act, 2002” Chartered Secretary, July 2006.pp1024-1027.
- T. Ramappa “Competition Act, 2002 – Some Points to Ponder” Chartered Secretary, July 2006. pp1032-1034.
- T. V. Narayanaswamy “Amendments to Takeover Regulations” Chartered Secretary, July 2006. pp1050-1052.
- Naresh Kumar “SEBI Takeover Regulations – Vital Issues” Chartered Secretary, October 1999.pp315-317.
- SEBI: www.sebi.org.in
- www.mergersindia.com.