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A Study on Merger & Amalgamation of Companies under Companies Act, 2013

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Abstract: **Change in the company or a business organization on a continual basis is a normal phenomenon. Mostly such a change is forced upon the company by external environment in the form of a new and efficient technology, emergence of a new competing product or a new market, increased competition or demographic changes and change in business cycles, etc. The companies undergo a change in the business structure to gain a cutting edge over the competition and to survive in the market by enhancement of goodwill and leadership. Technically, corporate restructuring is, "any change in the business capacity or portfolio that is carried out by an inorganic route or a change in the capital structure of a company that is not a part of its ordinary course of business or any change in the ownership or control over the management of the company or combination thereof".[i] There are several strategies of corporate restructuring namely merger, acquisition, demerger, joint venture, reduction of capital, buy-back of securities, consolidation and delisting of company.**

Keywords: **Companies under Companies Act, 2013, Merger & Amalgamation**

I. NON-ORGANIC RESTRUCTURING

In most of the literature, it is referred to as the restructuring of a corporate body where there is a third party element involved, for example, formation of a company to carry the business of a corporate body or the two parties coming together through a joint venture agreement or sale of an undertaking or demerger, or acquisition of another company either through friendly or hostile takeover, or amalgamation of one or more companies with the corporate body or merger of the corporate body with another company.[ii]

Amalgamation

Amalgamation is blending of two or more existing undertakings into one undertaking, the shareholders of each blending company becoming substantially the shareholders of the other company which holds blended undertakings. There can be amalgamation, either by transfer of two or more undertakings to a new company, or by the transfer of one or more undertakings to an existing company.

Merger

Merger is a form of amalgamation where all the properties and liabilities of transferor company gets merged with the properties and liabilities of the transferee company leaving behind nothing with the transferor company except its name, which also get removed through the process of law. The assets and liabilities of the merged company are acquired by the acquiring company. It is an amalgamation or absorption of two or more companies into a single entity. A merger should not be equated to consolidation, whereby two or more companies come together to form an entirely new company. But many authors have a disputed opinion regarding merger and consolidation respectively and have used the term interchangeably. The best approach to look at merger and consolidation is using the classic example of Company A and Company B. In a merger, A + B = A, where B is merged into A, but in a consolidation, A + B = C which results into the formation of an entirely new company known as C. But due to contrasting views with respect to merger and amalgamation, the terms are used interchangeably.[iii]

Valuing a Transaction and Consideration for Merger

The basic formula for calculating enterprise value is *base equity price plus the value of the target's long term as well as short term debt and preferred stock less its cash*. Base equity price is *difference between the total price and the value of the debt*. The buyer will be the company issuing shares in exchange of the shares of the other company or it will be a company with large market capitalization.[1]

The transaction of merger may involve cash, securities or a combination of cash and securities. The securities may include debentures and common stock as well as preferred stock. Stock transactions are preferred as they offer tax benefits as compared to the cash transactions. Merger payments can be in the form of fixed compensation or variable payments or payment in installments. In CVR mode of payment, future value is guaranteed if the shares of the acquirers in exchange for the shares of the target fall below a threshold. In the holdback provision, a specific part of the compensation in withheld and utilized on the occurrence of certain events.[2] Certain factors which have increased the merger activity in the recent years are summarized below:

- Change in technology has gained pace;
- Cost of transportation and communication have been reduced;
- Market has become internalized;
- Extensity, intensity, velocity and impact of globalization has increased;
- Forms and sources of competition in the market has increased;

[1] *Id*.

[2] *Id*. at 16.

- Regulations as well as deregulations have increased;
- Favorable market condition has existed post 1990's till early 2000's;
- Disparities between income and wealth have been broadening.

There is an increase in valuation relationships and equity returns for most of the 1990s which shows a significant rise as compared to the long term historical patterns. There are major favorable changes in the international market and problems have developed in the individual economies and industries.[3]

Mergers are often kept in three categories:

Horizontal Merger

Merger of two competitors is referred as horizontal merger. It involves the merger of two firms producing similar kind of product. In the year 1998, a $78.9 billion megamerger was concluded between Exxon and Mobil, two major petroleum companies. Another megamerger occurred when Wyeth was acquired by Pfizer in the year 2009 for $68 billion. Horizontal mergers are even termed anti-competitive due to increase in market power which would cause negative effect on the existing competition in the market.[4] Merger of Birla with L & T in the cement industry and merger of Jet Airlines with Air Sahara in the aviation industry are of the nature of horizontal merger.[5]

Vertical Merger

Combination of companies having buyer-seller relationship is called as vertical merger. Such merger takes place between enterprises in different stages of production and supply. Medco Containment Services, marketer of discount prescription medicine was acquired by Merck, one of the largest drug company in the year 1993 for $6 billion which enabled Merck to become the largest integrated producer and distributor of pharmaceutical.

Conglomerate Merger

Merger between companies who are neither competitor nor have a buyer-seller relationship are called conglomerate mergers. Such merger took place when a tobacco company, Philip Morris acquired General Foods for $5.6 billion in 1985.

Co-generic Merger

In co-generic merger, the two companies are in same or related industry but do not offer same products. They may share same distribution channels and offer related products, thus offering synergy.

II. MERGER & AMALGAMATION UNDER COMPANIES ACT, 2013

The Companies Act, 1956 was amended and a modified Companies Act, 2013 came into existence. The sections of Companies Act, 2013 dealing with Compromises, Arrangements and Amalgamations have been notified. Section 434(1)(c) of Companies Act, 2013 read with Companies (Transfer of Pending Proceedings) Rules, 2016 and Companies (Removal of Difficulties) Fourth Order, 2016 have also been notified on December 7, 2016 with effect from December 15, 2016. All the proceedings pending before any District Court or High Court will be transferred to the concerned bench of National Company Law Tribunal (NCLT).[6] NCLT will provide a regime of faster resolution of corporate disputes, which would ease the operation of companies and eventually reduce the burden on the courts. Though, there are certain proceedings which have been reserved by the High Courts and have not been transferred to the NCLT.

The pertinent provisions with respect to Mergers have been briefly explained:

1. Appointment of a Company Liquidator

A company liquidator would be appointed by National Company Law Tribunal (NCLT) in the event of compulsory winding up and by the company or its creditors during voluntary winding up of a company respectively.

2. Incorporation by Fraudulent Means

NCLT is empowered to remove the name of a company from the register of companies, upon receiving an application to that effect, if the same has been incorporated by fraudulent means. NCLT can even pass an order for winding up of such companies.

3. Disclosures

The entity proposing a scheme of arrangement or compromise has to disclose the same to NCLT, if the scheme includes reduction of share capital of the company or a Corporate Debt Restructuring Scheme consented by not less than 75% of the secured creditors in value. A notice for scheduling a meeting of creditors or members must be sent to the Central Government, Income-Tax Authorities, Reserve Bank of India, Securities & Exchange Board of India, Registrar of Companies, respective stock exchanges, Official Liquidator, Competition Commission of India and other authorities, if any, likely to be affected by such arrangement or compromise.[7] The authorities can make representation within a period of thirty days from receipt of such notice. Approvals were only required to be obtained by the creditors and the shareholders under Companies Act, 1956.

4. Disclosure of Valuation Report[8]

A valuation report prepared by a registered valuer of assets of the company should accompany the Corporate Debt Restructuring Scheme. The valuation report should also contain a notice of the meeting. Companies Act, 1956 was silent on disclosure of valuation report to the stakeholders. Disclosure of valuation report to the shareholders and the creditors have been made compulsory for better transparency and accountability under Companies Act, 2013.

5. Publications

All the relevant documents and the notice of meeting of creditors or members must be published on the website of the company as well as in the newspaper. Such documentation

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[3] GAUGHAN ET AL, MERGERS AND ACQUISITIONS 3-5 (TATA MCGRAW HILL ED, 2002).

[4] *Supra* note 34.

[5] *Merger & Acquisition, available at* http://www.legalservicesindia.com/article/article/mergers-and-acquisitions-1569-1.html (last accessed on January 10, 2018).

[6] Co. Act, 2013, §434(1)(c).

[7] Co. Act, 2013, §230(5).

[8] Co. Act, 2013, §232(2).

should be sent to Security Exchange Board of India and the concerned stock exchange in a listed company.

6. Buy-back of Securities

In the cases of compromise & arrangement involving buy-back of securities, approval of NCLT is required and it must be carried according to Section 68 of Companies Act, 2013.

7. Right to raise objections[9]

Any objection to scheme of compromise or arrangement will only be considered if raised by any individual or individuals holding minimum of 10% of shareholding or by persons having outstanding debt amounting to at least 5% of the total outstanding debt in the company. Such mandate would prevent frivolous objections to the scheme of compromise or arrangement.

8. Fast-track Merger[10]

A separate provision for merger of two or more small companies or between holding company and its wholly-owned subsidiary is provided in the 2013 Act. Section 233 of the 2013 Act provides a simplified fast track procedure for merger. It requires the consent of shareholders holding 90% in value and creditors representing 9/10th of debt in value along with the approval of the Scheme by the Regional Director, MCA. If NOC is obtained from Official Liquidator and Registrar of Companies, approval from Tribunal is not required for such mergers.

9. Purchase of Minority Shareholding

The notified provisions provide a mechanism to enable the acquirer of the prescribed shareholding in a company to squeeze out the minority shareholding at a fair price. The provision is attracted where the acquirer or a person acting in concert with other acquirer becomes registered holder of ninety percent or more of the issued share capital of the company or any person or group of persons becoming ninety percent majority or holding ninety percent of the issued share capital of a company.

10. Postal Ballot System[11]

The system of postal ballot has been an innovative step to ensure casting of votes in the meeting for or against the scheme. This will enhance participation of the shareholders and the creditors who cannot be present in the meeting on account of being outside the country. Further, in the 1956 Act, vote could only be cast either in person or proxy.

11. Compliance with the Accounting Standards[12]

An auditor's certificate certifying that there is no deviation from the accounting standards while conducting accounting treatment for valuation of the company has been made compulsory both for listed as well as non-listed companies.

12. Merger of a Listed company into an Unlisted company[13]

The merger of a listed company with an unlisted company will not automatically convert the unlisted company into a listed one. It will operate as unlisted company until and unless the requirements of SEBI and the applicable listing regulations are complied with. The Indian securities framework provides a stringent environment for granting of approval of any company intending to be listed. The Indian securities law prescribes strict enforcement of listing requirements by companies intending to get listed. SEBI had, however, eased these requirements for listed companies proposing merger by granting them exemptions from complying with initial public offering requirements as prescribed in Rule 19(2)(b) of Securities Contracts (Regulations) Rules, 1957 on a case-to-case basis. SEBI had issued guidelines in *circular nos. CIR/CFD/DIL/5/2013 dated February 4, 2013 and CIR/CFD/DIL/8/2013 dated May 21, 2013* stating that if the Scheme provides for listing of shares of an unlisted company without complying with the initial public offering requirements, then, upon court approval of the Scheme, the unlisted company has to file a specific application seeking exemption from SEBI. Such an application has to be filed upon, *inter-alia*, allotment of equity shares to the holders of securities of the listed company. The changes under the 2013 Act are in line with SEBI requirements. The 1956 Act was silent on this aspect.

13. Cross-border Merger[14]

Cross-border mergers are permitted between a company registered under Companies Act, 2013 and a company or a body corporate incorporated outside India. The foreign company may or may not have a place of business in India, but such foreign company shall be incorporated in such countries as may be notified by the Central Government. However, such mergers require prior approval of the Reserve Bank of India and the payment under the scheme can be made either in cash or in depository receipts or mix of both.

III. MERGER TRENDS- GLOBAL AND INDIAN EXPERIENCE

The merger and acquisition movement picked up pace in the early 2000s. The recession and the economic halt in United Sates and other parts of the world in 2001 slowed down the progress experienced in the merger market and brought an end to the fifth merger wave. But later, from 2003-2006 merger volume started rising in United States as well as in Europe. In the year 2007, the merger deal volume started declining in Europe, but it kept on rising in United States. But later in 2009, the merger market began to signal signs of rebound.

Even during the economic slowdown, there were bidders with stable and strong balance sheet and extensive cash reserves who were exploiting the opportunities in the weak merger and acquisition market. The same pattern was observed in Australia where the deal volume rose in 2003 but started declining in the year 2008 and 2009. Due to numerous restrictions on deals in China, A relatively different pattern was observed in China due to numerous restrictions on merger deals. The merger deal volume depicted a rise in 2008 with a sudden decline in the year 2009. Even in India and South-Korea, the deal volume expanded in 2003 with a slowdown in the year 2008 and 2009 due to global recession.[15]

[9] Co. Act, 2013, §230(4).

[10] Co. Act, 2013, §233.

[11] Co. Act, 2013, § 230(6).

[12] Co. Act, 2013, §232(3).

[13] Co. Act, 2013, §232(3)(h).

[14] Co. Act, 2013, §234.

[15] PATRICK, *supra* note 40.

A strong foreign investment flow was witnessed by the Indian economy towards the end of FY 2012-2013 which had positive effects on the Indian rupee and the Indian equity market with the existence of slight market and governance concerns. The financial and market conditions also showed positive stimulus towards monetary and liquidity concerns. [16] Transaction volume too depicted an inclining movement. The economic crisis of the year 2013 proved to be one of the worst crises after the Great Depression of 1930 which the world economy faced. There were signals that India and China would remain insulated from the crisis, but they equally got engulfed in the crisis. The number of restructured advances as a total percentage of gross advances increased from 3.5% in March, 2011 to 4.7% in March, 2012.[17]

IV. CONCLUSION

The increase in the practice of merger and amalgamation and other strategies of corporate restructuring specifically, acquisition, takeover, joint venture has multiplied the instances of cross-border insolvency. Corporate restructuring practice can be considered as a rescue measure for a company in distress. There is no guaranteed success of a merger deal and the basic reason for failure of any merger is due to the existence of cultural differences which is mostly ignored by the organizations. Huge cultural differences between the organizations are not taken in to account by the management. Moreover, the companies expect high growth from the merger and consider merger or any other corporate restructuring, a solution to their financial distress. Proper research and analysis has to be done before undergoing merger of any two organizations.[18] Moreover, for any entity in distress, merger of the distressed entity to a healthy entity will not always give a positive result. It may be possible that the scheme of merger is not a feasible one and the present state of affairs is reflecting that the merger won't be a profitable one for either of the company. The most important role in a merger scheme is of the deal makers who are responsible for making realistic schemes which would enhance efficiency of the organization and result in successful integration of the two companies. After the wave of liberalization in 1991, the merger deals in India have been continuously rising. Around 126 merger and acquisition deals were entered into between Tata Group from the period 1998 to 2008. In the Indian context, such merger and acquisition deals saw a decreasing trend from 2008 due to the global crisis, but the trend of merger suddenly started to show a rise in 2010 when the telecom sector recorded the highest activity with major deals like Vodafone- Hutch Essar and Tata Tele- NTT Docomo. The international legal framework related to mergers in India has also evolved over-time. Indian courts and tribunals are showing inclination towards international principles and practices.
The Companies Act, 2013 has brought several modifications in the provisions governing compromises, arrangements, reconstruction and amalgamation. Though, most of the sections are similar in content but the provisions as contained in the 2013 Act are robust which has simplified and streamlined the process of compromises, arrangements and amalgamations. The notified provisions are promoting good corporate governance practices by bringing transparency and accountability in the form of additional disclosures.

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[i] *Introduction to Corporate Restructuring, available at* http://corporaterestructuringfundamentals.blogspot.in/2011/01/introduction-to-corporate-restructuring.html (last accessed on January 9, 2018).

[ii] *Introduction to Corporate Restructuring, available at* http://corporaterestructuringfundamentals.blogspot.in/ (last accessed on January 10, 2018).

[iii] PATRICK A. GAUGHAN, MERGERS, ACQUISITIONS, AND CORPORATE RESTRUCTURING 3-13 (2011).

[16] *IMF Global Financial Report, 2013,* http://www.imf.org/External/Pubs/FT/GFSR/2013/02/ (last accessed on January 5, 2018).

[17] *Ibid.*

[18] *Failure of Merger and Acquisitions,* http://business.mapsofindia.com/finance/mergers-acquisitions/failure.html (last accessed on January 8, 2018).

