Mergers, Acquisitions and Corporate Restructuring
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Lecture – 04
Legal Environment of M and A in India

Hello friends in the previous session you talked about mergers, acquisition in general and merger, acquisition is a strategy for growth of the companies, but we understand that since mergers, acquisitions involve corporate sector in that case there are several laws and regulations which affect the corporate sector. Similarly, there is a specific laws, regulations with respect to mergers, acquisitions in India as well as in other countries.

So, in this session we will talk about the legal environment affecting the mergers, acquisitions particularly with reference to India as such.

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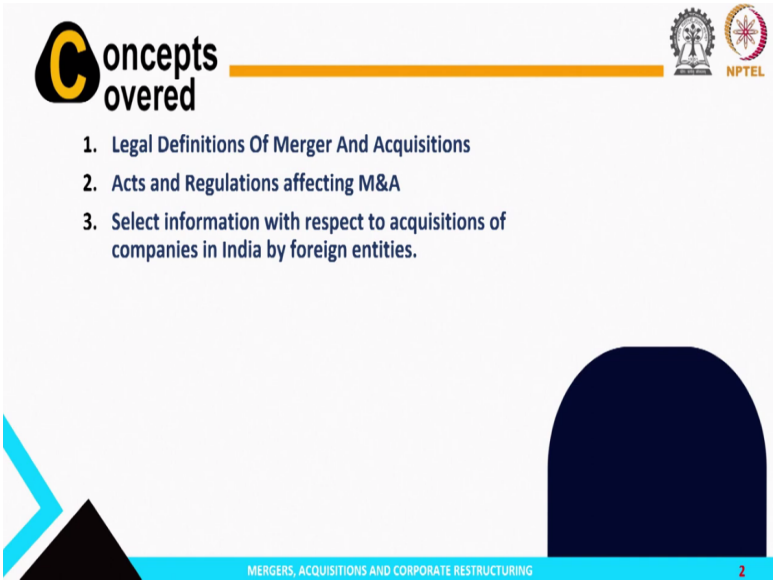

So, we will be having these concepts like legal definitions of merger, acquisition although we defined those merger, acquisition generally in the previous sessions, but here we will talk with respect to the specific act in case of India. We just talked about salient features or points given by different laws and regulations with respect to merger, acquisitions. We also discuss certain information with respect to acquisition of companies in India by foreign entities.

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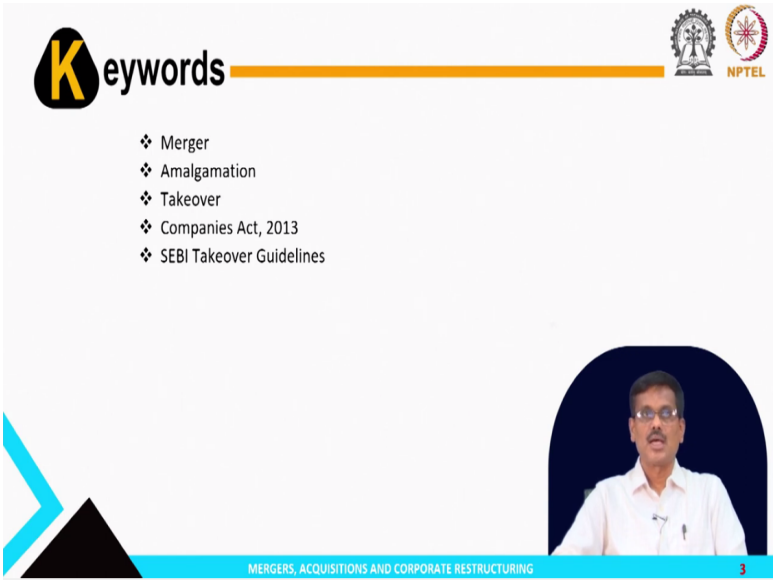

So, the keywords, merger, amalgamation takeover, we will talk about Companies Act 2013 related to provisions and also we will discuss partly about SEBI takeover guidelines. One of the point let me mention here is that we will be having separate exhaustive session with respect to legal aspects of mergers, acquisitions. So, this session is only going to talk we discuss about the nuances of different acts and regulations as a mergers, acquisitions in India as such.

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So, there are different like we say when you purchase some item in the market so it is given that buyer be aware. It is the buyer who has to satisfy himself or herself that what is the things he or she is purchasing as such. We may not be blaming the seller as such in that case. So, when the companies is being acquired the acquirer should know what is there in the target

otherwise it will be a problem at the time of integration of the company, the target with the acquisition acquiring company.

So, there will be no time we cannot go back and to reverse a decision. So, a buyer or the acquiring company or the merging entity should be aware about different legal aspects in case of merger, acquisition. So, one is that yes the Companies Act talk about different rules and regulations of a company's governance and company registration and different other things are there.

So, the Companies Act also had certain provisions with respect to mergers, acquisition and amalgamation and takeover etcetera. So, in that case all the rules and regulation with respect to M and A and other things has to be followed by the companies who are going for mergers and acquisition. Then there could be certain things with respect to shareholding pattern and issuance of securities.

Then merger and acquisition can lead to issue of new securities in that case the respective guidelines of securities issue has to be followed and similarly compliance with tax laws. Tax laws could be related to income tax or the indirect taxes like GST. So, when the merger, acquisition takes place so we have to see that the tax laws are followed typically the Income Tax Act of India they have certain provisions with respect to amalgamation.

And the company have to follow those rules and regulations because there are certain things, certain merger, acquisition maybe beneficial from the tax point of view. In that case the companies have to follow the relevant rules and regulations of tax laws. Then there could be something related to financing regulation certain like foreign investment guidelines could be there and when you raise funds from different sources there could be some regulations.

So, we also follow the regulation related to financing of this, it could be also related to equity issues. If he is going to follow out a merger acquisitions then companies will have different contracts entered with the employees of the organization including key managerial personnel, could be CEO, could be the directors of the company also outside parties. So, those things also we have to look at.

Of course, we will be discussing more about this in our subsequent session and due-diligence, but still as a M and A party one has to see that the contracts are actually enforced and there is no violation contracts done by the target company or the merging companies with outsiders or the insiders for that matter then we have a Competition Act in India and we have to also comply with the Competition Act provision when it becomes applicable depending on the cases of mergers and acquisition.

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Then the companies when they go for loans from different institutions, financing agencies or banks there could be some agreements or contracts between the financer and the company that the borrower and the financing company of the bank as such and that may involve different mortgages, pledges, guarantees. So, we have to see that those things are also ensured and they are also followed.

And any legal obligation is there for the target company point of view they have to kept intact till the loans are actually repaid by the new entity or the merging entity as such. Then for business operations where the companies may have certain license and permits, for example, in case of telecom sector so you have the 3G, 4G or 5G licensees taken from the government of India.

In that case there are certain do's and don't, certain regulation that govern the usage of licenses. So, those also have to be followed or in case of merger in the case of telecom companies. Similarly, other sectors like insurance sector has its own regulations, banking

sector has its own regulations, license etcetera. In that case those things also we have to see that they have followed as per the law.

The companies may be involved with international trade in terms of imports and exports. So, there are certain regulations with respect to import and exports from the government of India and those guidelines also have to be followed so that there is not violation of that. Companies may have intellectual property rights they are very sensitive issues. So, it should not be so that the intellectual property rights are not protected and there is a violation of that.

So, there is somebody who may complain later there is infringement of intellectual property rights. So, the companies have to ensure that intellectual property rights are actually ensured as far as those rights are concerned and there could be different legal documents in the company where we may have certain provisions they have to be followed and nowadays the environment law wise everybody is very sensitive as well as the regulations are very strict now.

So, it depends on the type of company, for example, there is a pharmaceutical company they will be subject to certain environmental regulations and we have to see that those M and A regulations are actually followed as such and there is also possibility, there could be some cases in the court of law pending against the company or the target company might have filed a case.

So, one has to take cognizance of that and accordingly make the provisions so that the companies the acquiring companies also prepare if the cases are still pending and continuing after the merger, acquisition because just because the target has been merged the cases will not vanish, the cases will continue and legal cases. So, that has to be resolved in the court of law.

So, till that time the acquiring company will be responsible for that. So, unless it is resolved before the acquisition, so one has to see that these cases are taken care in the court of law as per the regulations. So, these are the basic summary not exhaustively that there is nothing else, it is not like that. There could be several other things, but we have to just summarize that this could be main provisions in case of different acts and regulations governing the companies in India as such.

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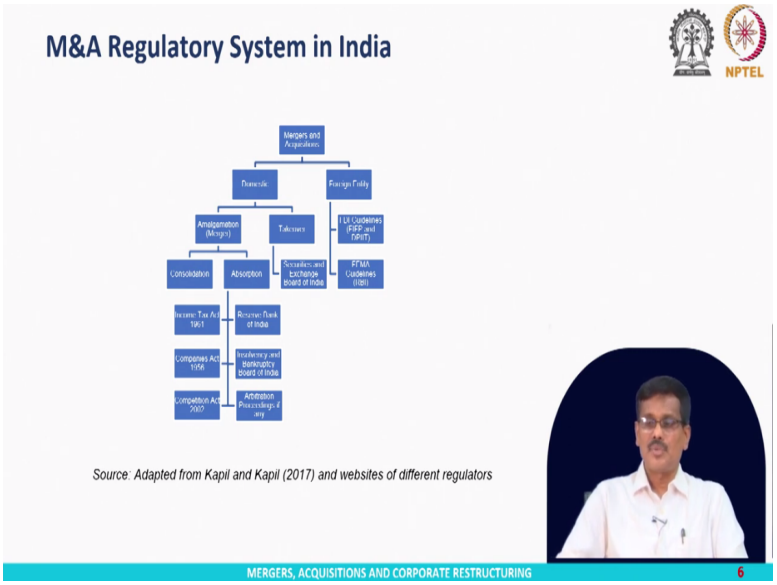

Then we go to the overall framework in that case you have got mergers, acquisitions. We have classified them into two parts that is domestic acquisitions and foreign entity. As far as domestic entities are concerned we have got amalgamation or merger that is given as per the Companies Act is defined that or we can also have in that amalgamation merger we can have a consolidation.

So, few companies come together in the group and have a single entity. Absorption means there is one company actually gets absorbed by the acquiring company. So, one company cease to exist in that case there are several acts like Income Tax Act certain provisions are there then Companies Act as you discussed earlier it has certain provisions with respect to mergers, acquisitions, Competition Act has its provisions.

And if it is a banking and finance sector company that RBI guidelines will be useful, will be applicable and nowadays we see that the insolvency and bankruptcy board of India with its insolvency code there is a enabler that the bankrupt companies can also be taken over by other companies. So, it has revived because in the bankruptcy takes place the system wants that the company should continue because there are several stakeholders interest is actually involved.

In that case the resolution professionals may look for entities which can actually takeover this bankrupt companies, in that case the IBBI codes will be applicable and then there could be also problems involving different companies where there could be arbitrations. Typically,

what happens if there is a deal already signed between two companies and it is possible that one company may back out.

In that case in prior to this they sit together they might that is there any problem we may go for arbitration. There could be international arbitration typically happens in case of a foreign entity versus an Indian entity there is some deal and there could be enabler that if there is any problem they can go for arbitration. So, similarly there could be a cases where the companies might have agreed to go for acquisitions and mergers typically involving two companies in two different countries.

And for some reason one of them back out in that case the other party may go to international arbitration and for filing a case so that the case is resolved and accordingly the things are taken care. So, in that case when you are acquiring a company which involves the arbitration procedure pending you cannot say that you have to be also be careful about that and you have to take care of those arbitration proceedings.

That is going to affect the merger acquisition in that case and coming to the foreign entity we have FDI regulations where you have got now these days your new regulations, new enablers have come for Foreign Investment Facilitation Portal that is FIPP and we have another called Department of Promotion of Industry and International Trade we have given in the subsequent styles we have given the full form.

So, these two things will be applicable in case of foreign entity and of course DPIIT is also applicable for Indian company not necessarily only foreign companies for that matter and then the Foreign Exchange Management Act also guideline which is typically taken care by the Reserve Bank of India in case of foreign acquisition by foreign companies also in case of acquisition of foreign companies buy Indian company. So, FEMA guideline also have to followed.

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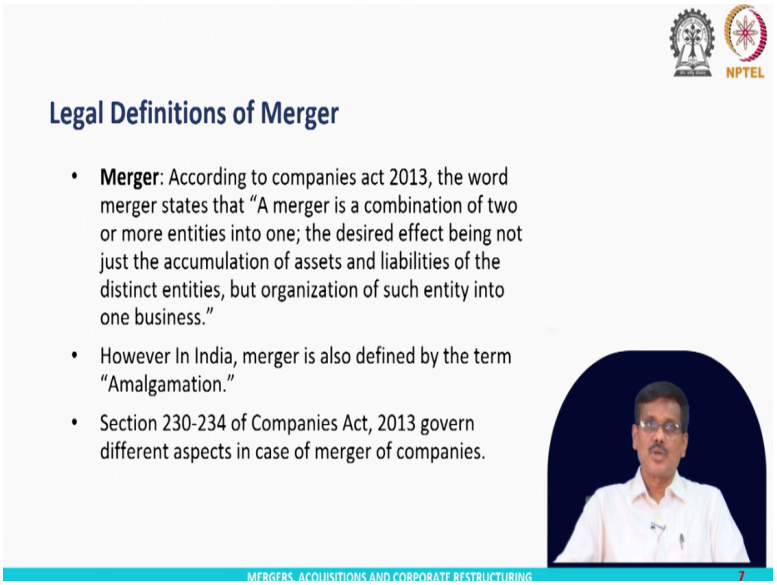

So, going to the next thing where you talk about the legal definition of merger here. So, the Companies Act 2013 the merger is defined and they say that merger is a combination of two or more entities into one and it is just not accumulation of assets and liabilities it becomes one business. So, just not the assets are more the liabilities are not we wait together. It becomes single business as such.

And this in India also we use in fact in the earlier version Companies Act the Companies Act 1956 the term was amalgamation. Now in new Companies Act, 2013 they say merger or amalgamation as such and Section 230 to 234 of the Companies Act of 2013 govern different aspects of M and A in India as such the merger of companies in India as such. We will discuss in more detail about these sections in the legal aspects M and A session.

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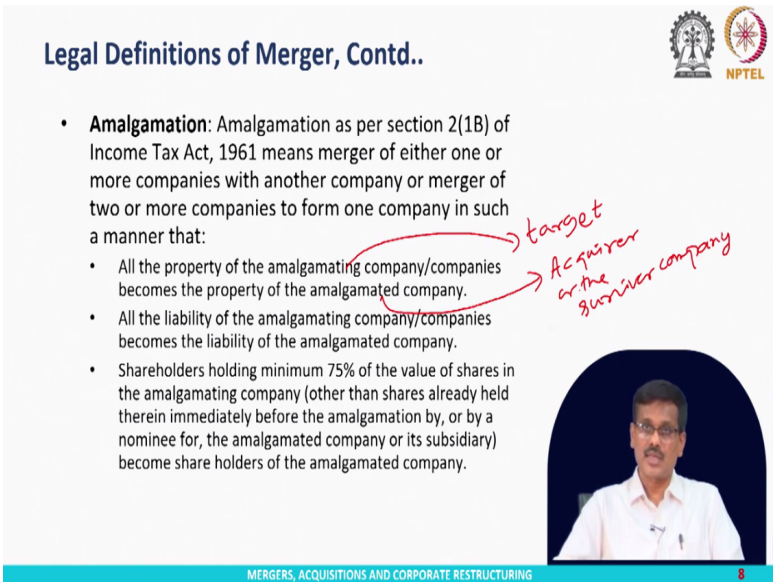

And then we go to the other aspects like in Income Tax Act also we have certain provisions. We may take advantage Income Tax Provision, but for that matter Income Tax Act defines the amalgamation as per Section 2 1 B of Income Tax Act 1961 which says that merger of either one or more companies with another company or merger of two or more companies to form a one company in such a manner that all the property of the amalgamating company becomes the property of the amalgamated.

So, when we say amalgamating and amalgamated as such amalgamated it could be in normal parlance we can say amalgamated as amalgamating could be taken as let us say in general parlance called target and amalgamated company could be taken as the acquirer or the survivor or surviving company. So, all the property of the amalgamating companies of the target companies becomes the property of that amalgamated or the acquiring company of the surviving company all of them.

Then all the liability also becomes the liability of the amalgamated company that my target company liability becomes the liability of the acquiring company and shareholders holding minimum 75% the value of shares in the amalgamating company become also shareholders of the amalgamated company. If these three conditions are fulfilled then it will be taken as a amalgamation as per Income Tax Act, 1961.

And there will be certain benefits because of this and which we will be discussing in some other slide for that matter. So, amalgamation definition or merger definition need not be same as per all the act. Income Tax Act defines or recognizes amalgamation taking place only these three conditions are fulfilled whereas in case of Companies Act the merger or amalgamation defined as such separately, but as a company both the regulation, both the rules have to be followed by them.

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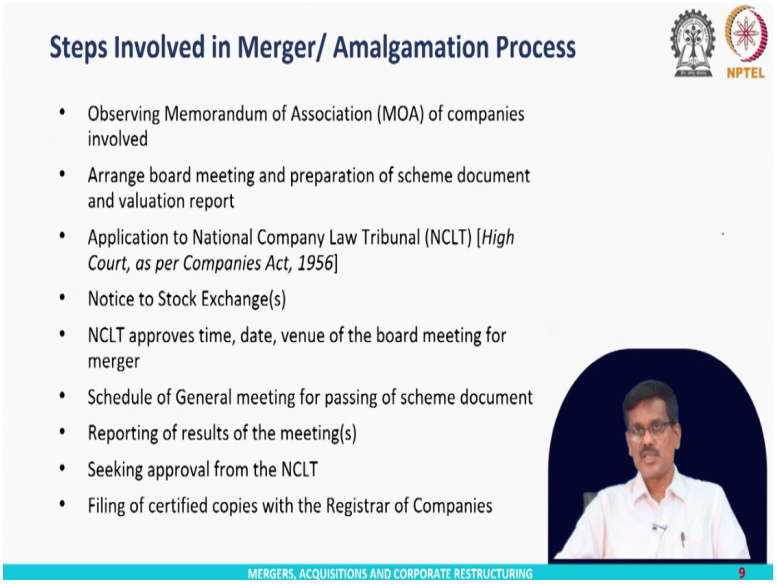

Then you talk about general process as a mergers and amalgamation process typically from the Companies Act point of view so we have to see that we have to observe something called the Memorandum of Association of company, any company which is formed there are two statutory documents to be submitted by the company when it is registered. They are called Memorandum of Association and MOA and Articles of Association.

Memorandum of Association has got certain clauses. One of the clause is objective clause, name clause is there, situation clause is there, liability clause is there, objective clause and different clauses are there, five different clauses are there. One of the important clause is in fact all the clauses are important that one of the clause is object. What is objective of the company, what do (()) (16:37) do?

Objective of the company could be to produce steel, objective of the company to provide telecom services whatever that maybe, the objective has to be mentioned and the companies has to do only those things. So, it is possible suppose target company becomes part of acquiring company target company does not exist now cease to exist and target company has certain businesses which was not done by the acquiring company.

In that case the Memorandum of Association of the acquiring company will not lead to those objective. So, when it becomes merger takes place where the target does not exist and target business will be done by the acquiring company which was not there as part of their business before acquisition in that case they have to amend the Memorandum of Association and then

only they can make it part because unless that object is mentioned in Memorandum of Association with a special three-fourth majority in the shareholders meeting.

They have to first amend the objective clause then only the M and A actually can take effect. So, they have to be careful about it so we have to observe them then you have to also have board meeting and you have to prepare a scheme document and valuation report also then the companies have to go the National Company Law Tribunal as NCLT which has got branches in different capital cities.

Earlier as per Companies Act, 1956 it was to be approved by the High Court of the particular location or particular state. Now, High Court role is taken of the National Company Law of Tribunal which also takes care of several other things which led to companies management as such like insolvency proceedings also taken care by the NCLT now then you have to give the notice to the stock exchange if it is listed.

And then NCLT will approve give a time when the date and venue the date the board meeting can take place then board meeting will also say that as well as general body meeting has to come to the shareholders have take place where they have to arrange both the companies has to approve the scheme document in the general body meeting and once these general body meeting passes that these things have taken care they have been passed and merger will take place then it will be reported to the NCLT and NCLT will now approve.

And once this is approved then all the certified copies has to be filed with register of companies. In nutshell, these are the steps, but there could be so many other steps in between, but these as per the Companies Act provisions these are the steps to be followed by in case of mergers and acquisition.

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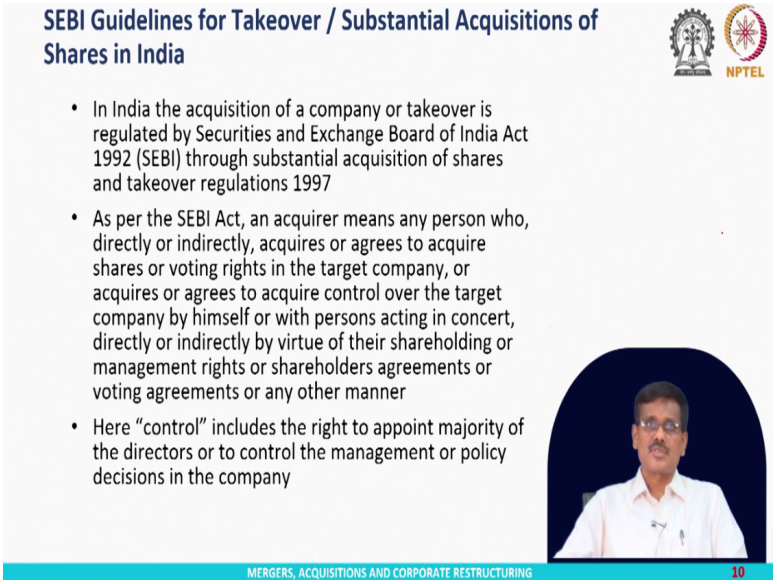

Then you have got Securities and Exchange Board of India which has got certain guidelines of takeover and substantial acquisition of shares and in India the acquisition of company takeover is regulated by SEBI through something called substantial acquisition shares and takeover regulation 1997 and SEBI defines that acquirer could be any person who will be directly or indirectly acquires or agree to acquire shares or voting rights in the target company or acquirer agrees to acquire control over the target company by himself or with the person acting in concepts.

Person's could be company also need not be human beings for that matter it could be corporate form of concepts also directly or indirectly by virtue of their shareholding or management rights or shareholders agreements or voting agreements or any other manner. So, effectively they take the control over the target company and control need not be that you have got only if you have got let us say one may idea that control means having rights over 50% shareholding in a company that is not the control.

Control is that if you are able to select the majority of the directors to the board or control the management. It could be 30%, 20%, 35% for that matter of the step of that particular stake we are able to do that then you can be say that yes you have taken over the control it is not necessarily control means more than 50% voting rights in the company for that matter so that is the control with respect to SEBI guidelines.

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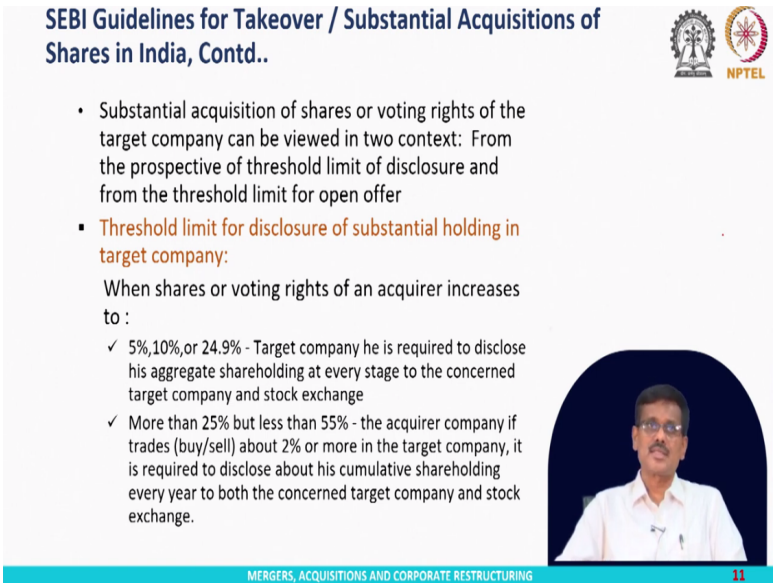

Then once the company substantially acquire the shares and the company has to actually notify the stock exchanges and the target then we have got this mistakes similarly of certain limits or threshold limits are there like you have got this 5%, 10% and 24.9% these are the points. So, once the company has a 5% stake in a particular company and the target let us say whatever.

Whether you want to acquire them or not because with 5% you have taken up your shareholding has become 5%. You have to inform the stock exchanges as well as the target company that our shareholding your company has become such and such percent. So, similarly we will become 10%, we will become 24.9% these things you have to notify them. What happens suppose you have not notified them.

And tomorrow the company's go for the hostile takeover of the target and then target company can see you in the court of law and say that you have not followed the due procedure because you are suppose to notify us you have not done that in that case the takeover attempt can be foiled because of legal provision as such. Similarly, more than 25% or less than 55% if you are going to acquire and you are acquiring further more than 2% each.

For every 2% acquisition of shares you have to also notify to the stock exchange as well as target company yes suppose you have become 25% it become 27% or 29% like that then accordingly you have to also inform these target company that our stake in your company has become such and such. We should expect the target company to come to know on its own that the shareholding has changed.

So, it is like a public disclosure when you disclose to stock exchange and along with that you have to also disclose to the concerned company. SEBI also has guidelines with respect to substantial acquisition of shares or voting rights where the acquiring company has to notify it to the stock exchanges and the target company. So, depending on the stake suppose once if company A acquires let us say just by simple market, open market purchase itself.

Suppose its stake become 5% of some other company the company has to notify the stock exchange of the target company then our stake in this company has become 5%. Then next notification at 10% then notification 24.9% after 25% with every 2% extra acquisition, extra holding in the target company it has to be disclosed to the stock exchange as well as to the target company.

So that the companies know that yes there is a acquisition by something and maybe it will give you signal to the general market that there may be one company is interested in this particular company. It should not come as a blind surprise tomorrow and suppose they have not notified and they then go for some open takeover hostile takeover of the target company, the target company can sue the acquiring company that you have not followed.

And they can sue in the court of law and that way the hostile takeover attempt can be filed, but the companies are supported by different legal experts. So such things very (()) (24:05) takes place, but this provision is anyway they are in the SEBI takeover guidelines.

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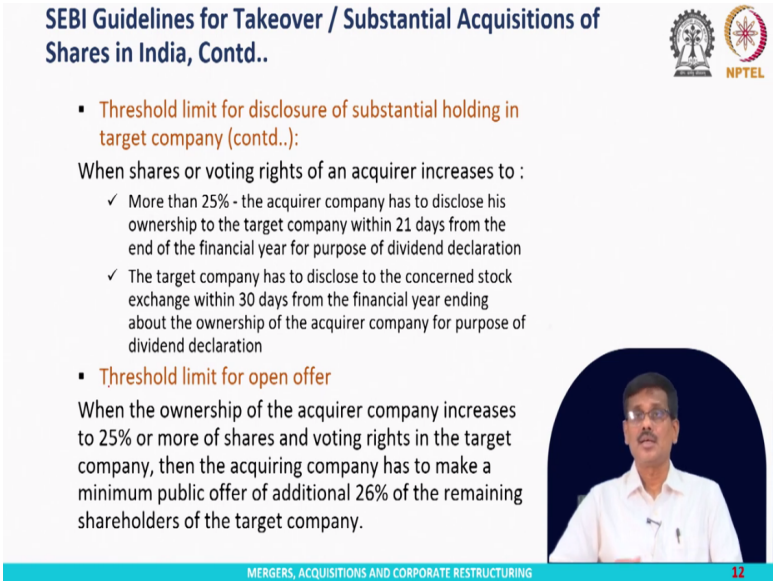

Then yes then you have threshold limit for disclosure of substantial holding target is continuing we continue that. Similarly, you have to suppose voting rights become more than 25% the acquiring company has to disclose the ownership target within 21 days from the end of the financial year and similarly we discussed talking about the within 30 days from the financial year ending about the ownership of the acquiring company for the purpose of dividend declaration.

Then if the ownership with the acquiring company increase the 25% or more in that case it is the obligation for the acquiring company to make a minimum public offer or additional 26% of the remaining shareholder of the target company. So, that other retail shareholders have an opportunity to exit which is possible that the company might have taken over some shares from the promoters giving a premium on this existing market price.

Now the ordinary retail shareholders, the minority shareholders also should get that benefit in that case the same thing also has to be given to the other shareholders so that they also take the part in the exit option maybe possible with a premium for that. So, there should not be added disadvantage.

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And then we have got the Competition Act 2002 that came off in 2002 and earlier we had its earlier version was Monopolies and Restrictive Trade Practices Act 1969 and the Competition Act 2002 became operational in 2009 although it was enacted 2002 and then we had the Competition Commission of India CCA which regulates the law and the operated by the Competition Appellate tribunal.

Any agreement between companies in areas of procurement, production, distribution of goods all those things your Competition Act is involved. It also regulates the anti-competitive agreements and abuse of dominant position. We will discuss about this in the legal aspects session when we will discuss each act separately so that they will ensure that the monopoly is not created as such.

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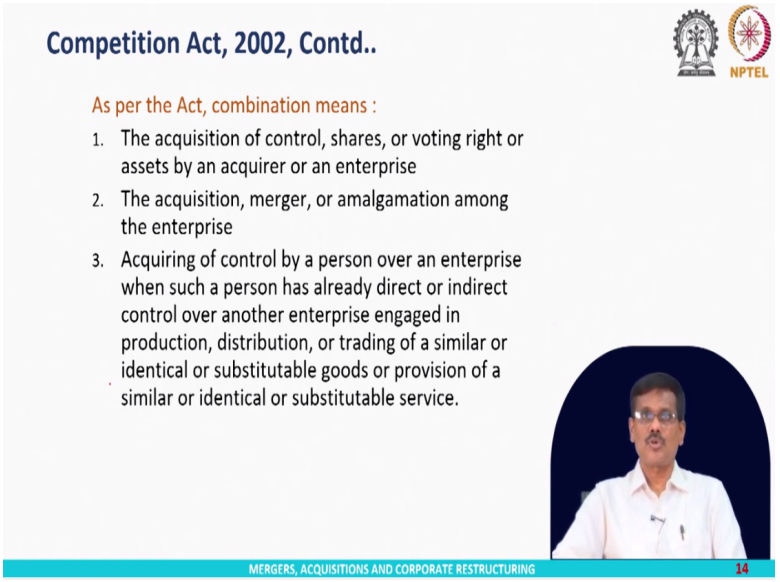

And then combination act also defines the combination where we say acquisition of control, shares or voting rights of assets when acquirer or enterprise. It can be acquisition, merger or amalgamation among the enterprise where the competition act will be invoked so that the unfair trade practices are not there and the acquiring company has no substantial control over the market for that matter.

So, this competition commission will ensure that their competition is ensured, choices are there for both consumers as well as suppliers. One company should not be in a substantial control position to control the market for that matter.

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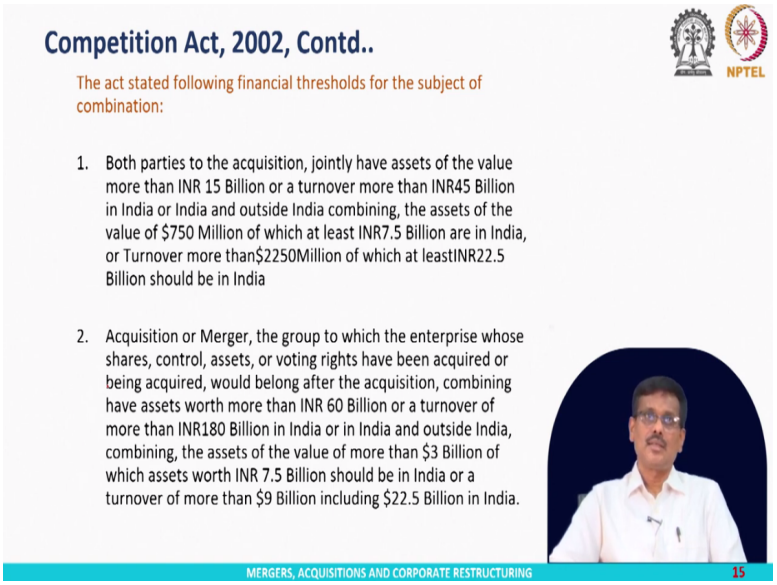

And then there are certain threshold limit where this Competition Act gets invoked. When the combined party together the assets become more than Rs. 15 billion or turnover becomes Rs. 45 billion in India or outside India also combining. Similarly the foreign companies company the asset becomes 750 million of which 7.5 billion in India and turnover more than $2,250 million of which at least 22.5 billion should be in India.

In that case the automatically is referred to the Competition Commission for approval. These are the threshold limit and acquisition of merger could be there the group to which the enterprise with shares and control assets of voting rights have been acquired or being acquired would be belong after the acquisition combining of an asset worth more than 60 billion or a turnover of more than 180 billion India or outside.

So, this has to be approved so that these are the threshold limit where the provisions of Competition Act gets involved that means competition commission has to approve the merger without that merger acquisition cannot take place.

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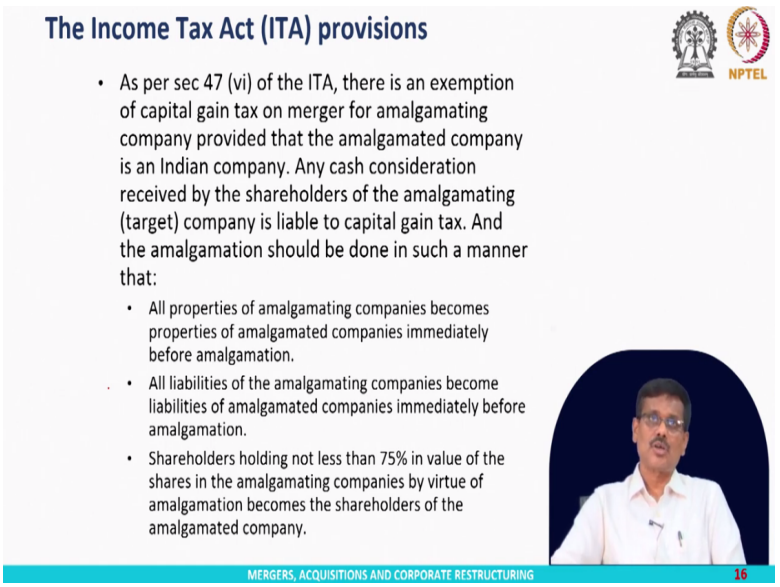

And you also have Income Tax Act we discussed about that in the previous some other slide and here actually three things I have talked earlier. This is called the target business is continuing as it is although it has become part of the acquiring company so that the companies can take advantage of any tax benefits otherwise it cannot take the advantage of tax (()) (28:35) or loss could be there in target company which you can combine and make some tax benefit for the acquiring company.

But only if these three conditions are fulfilled then it becomes amalgamation as per Income Tax Act then the acquiring company can take advantage of the Income Tax Act benefits for mergers and acquisitions. We will be discussing further about this in the subsequent sessions.

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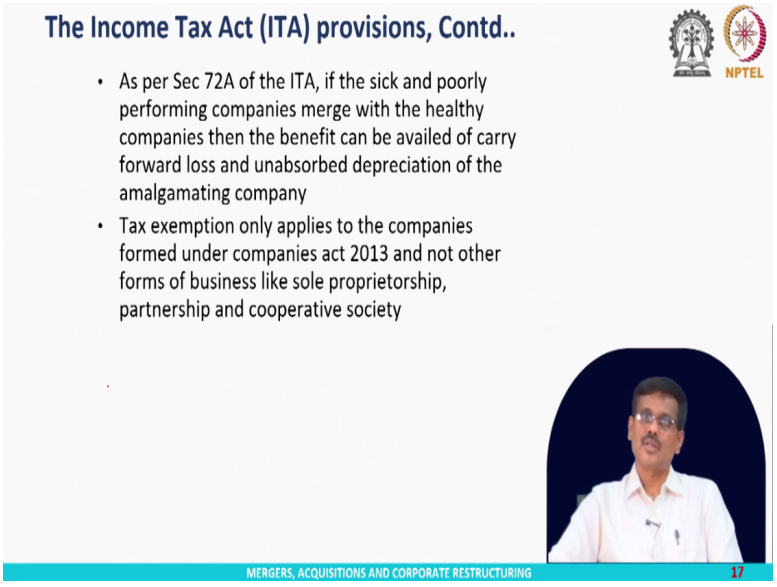

And yes as per 72 Section of the Income Tax Act sick and poorly performing companies also can merge healthy companies and the benefit can be availed the carry forward losses and unabsorbed depreciation of the amalgamating with the target company and tax exemption only applies to the companies formed under Companies Act 2013 and not any other form of business like sole proprietorship, partnership there we merger these tax benefits (()) (29:23) which is only applicable for the companies registered under the Companies Act of India for that matter.

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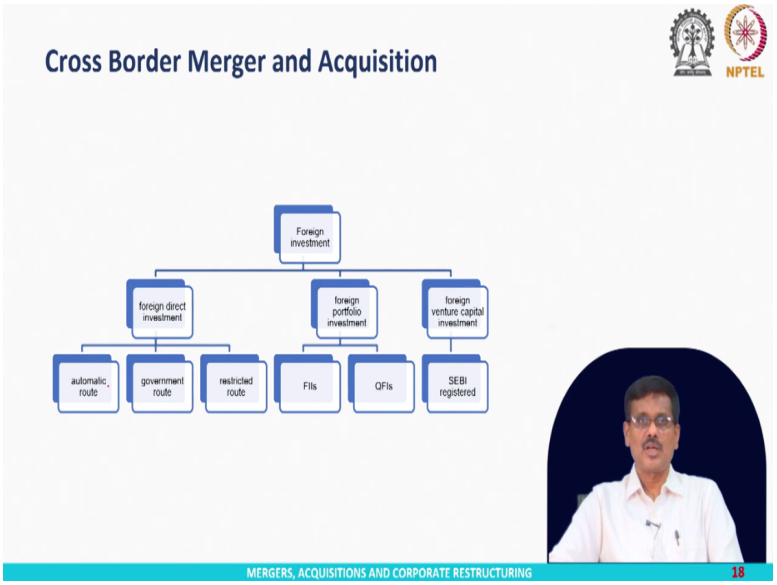

We have one also cross border acquisition where you have an foreign investment, you have foreign direct investment where you have got automatic route, government route, restricted route these are there when the cross border acquisition takes place. So, these are the way the companies can possibly acquire shares in Indian companies, it could be FDI, it could be FPI, it could also be through venture capital registered with SEBI also can acquire the shares in the company in India as such.

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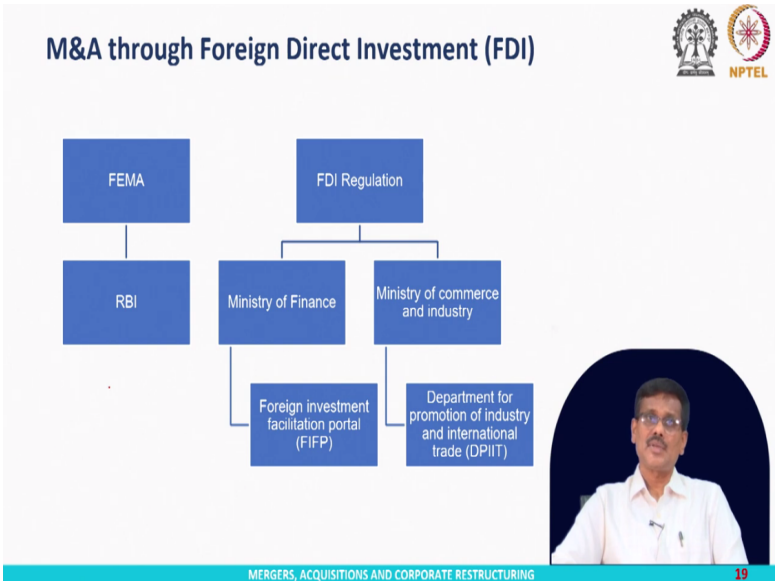

And in that case M and A through FDI there are certain regulations. You have FEMA guidelines to be followed of the RBI. Reserve Bank of India also ensure that FEMA guideline followed and FDI regulation is concerned, ministry of finance will ensure that FIPP Foreign Investment Facilitation Portal we have got now we have got a single window scheme for foreign investment they have to be followed.

And for ministry of commerce and industry we discussed earlier the Department of Promotion of Industrial and International trade those guidelines follow. They also actually facilitate the investment by foreign entities in India. So, when the foreign company is acquiring companies in India they have to ensure that the rules, regulations, procedures followed.

They should also take advantage of the facilities available those two provision like FIFP and DPIIT for that matter.

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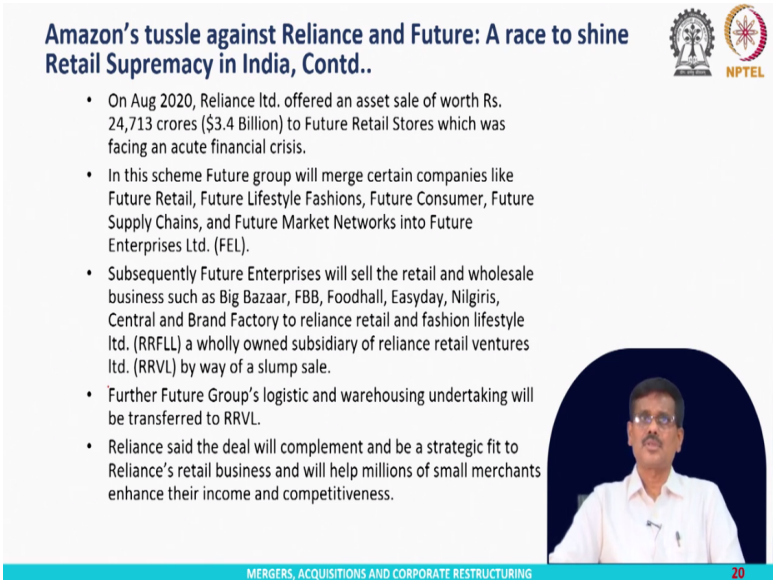

And we have one case here we have talked about recently. Amazon was suppose to acquire future group at Big Bazaar in between Reliance came and took place. There are so many things took place in this particular saga and in August 2020 Reliance actually offered an asset sale of 24713 crore in future retail which was actually facing lot of financial distress and future group was suppose to merge certain companies like future retail, lifestyle fashion, future consumers certain companies and into future enterprises.

Then subsequently futures enterprise will sell the retail and wholesale business like Big Bazaar, FBB, Foodhall, Easyday, Nilgiris all those the popular brands of Big Bazaar to Reliance group as such then logistics will also go to Reliance group. Reliance thought that it will be compliment and strategic fit because they are also going bigger in their retail business. So, this is going to augment their retail business for that matter and it is going to be scale of scope could be there.

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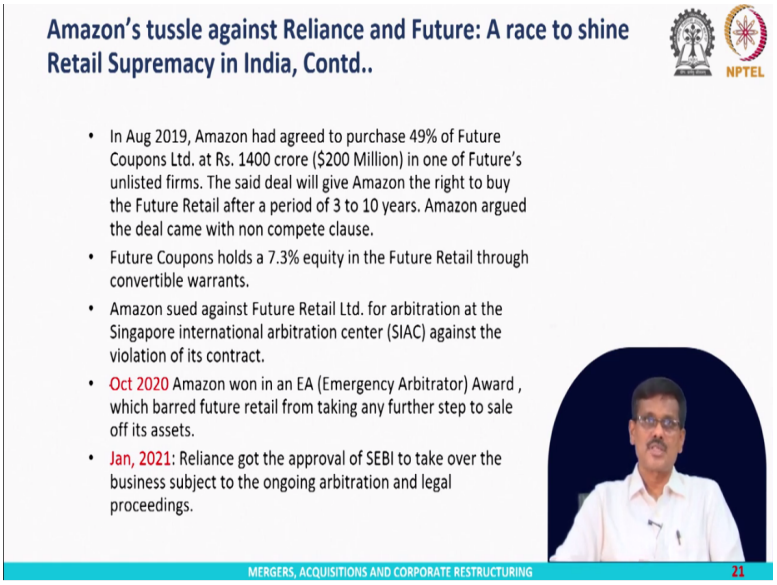

But there is a catch here where in 2019 Amazon has agreed to purchase 49% of future coupons in one of the futures unlisted firms and that was supposed to lead to acquisition of future group or future group Big Bazaar etcetera by Amazon itself. So, Amazon wanted to acquire future group by invest and future group have to take control over that and that was the agreement as such.

And in between these thing took place and so in October 2000 Amazon sued against future retail for arbitration in Singapore we talked about we have to also look at any arbitration pending in this case you can see the Reliance also now has to see that the arbitration taken care then only the merger acquisition can take place. So, lot of things have taken place. This is an example where you talk about how different legal issues are involved in case of company merger and acquisition particularly in a distressed company for that matter.

So, Amazon won and emergency arbitrated award which barred future retail from taking any further steps to sell its assets to maybe to Reliance or any company for that matter. So, Reliance also in the meantime got the approval from the SEBI to take over the business subject to this arbitration. So, the arbitration is taken care then the Reliance can obviously takeover the future group for that matter.

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Then in 2021 the Delhi High Court passed a order that yes future group can move to which will go to division bench then NCLT the case also going to National Company Law Tribunal. We dismissed the application by Amazon and allowed the future group to hold the meeting shareholder so that the assets can be sold to Reliance then Competition Commission of India also came into picture where they suspend the deal between Amazon and future whichever deal was there was suspended.

Then in February 25, 2022 unable to pay the lease rental Reliance in the meantime transfer certain assets of the future and the leases and took over certain stores from the future group that Big Bazaar group to them so they had some 1,700 stores of Big Bazaar and out of 500 stores are now taken over by Reliance.

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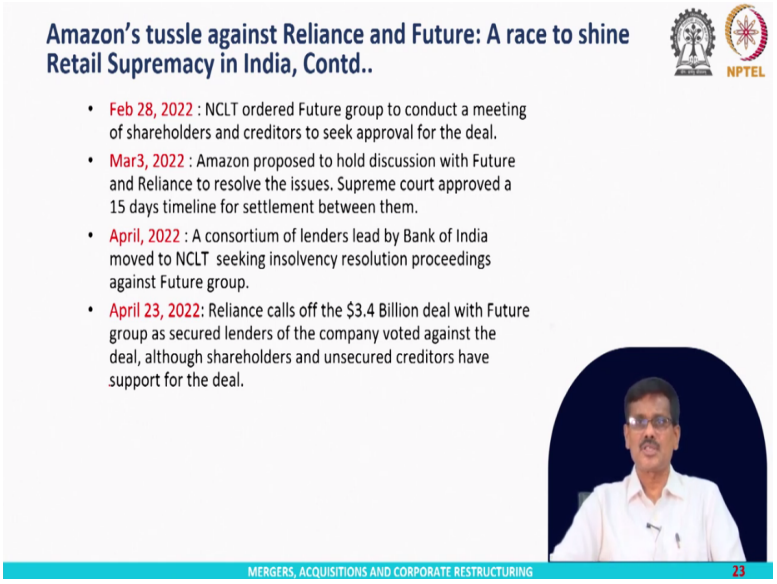

So, we can see in that case several things have taken place, several laws, regulations, several agency, regulators have come into picture in this case as such. So, in February 28 again NCLT order the future group to conduct a meeting of shareholders and creditors so that it can seek the approval for the deal and March 3rd then Amazon proposed to hold discussion in the future group and Reliance resolve the issues.

Supreme Court also has approved given 15 days time that. In April a consortium lenders in the meantime for the Bank of India laid by them. They also move to NCLT so that they can file an insolvency against the future group. Now, it has gone to insolvency board and which will decide the future group is insolvent or not then in the meantime with all these problems etcetera Reliance has now called up these deal with a future because secured lenders of the company voted against the deal.

They did not approve it because M and A deal also to approve the shareholders as well as creditors. So, creditor need to approve so Reliance has now called up that particular deal with the future group as such. So, this is you can see the case where it involves several agency, several regulations for that matter in case of mergers and acquisition and if it is a smooth selling if it is a healthy company possibly this so much complication may not be there it is smooth selling friendly acquisition.

All those things may not take place, but in case of distress company these things can always take place.

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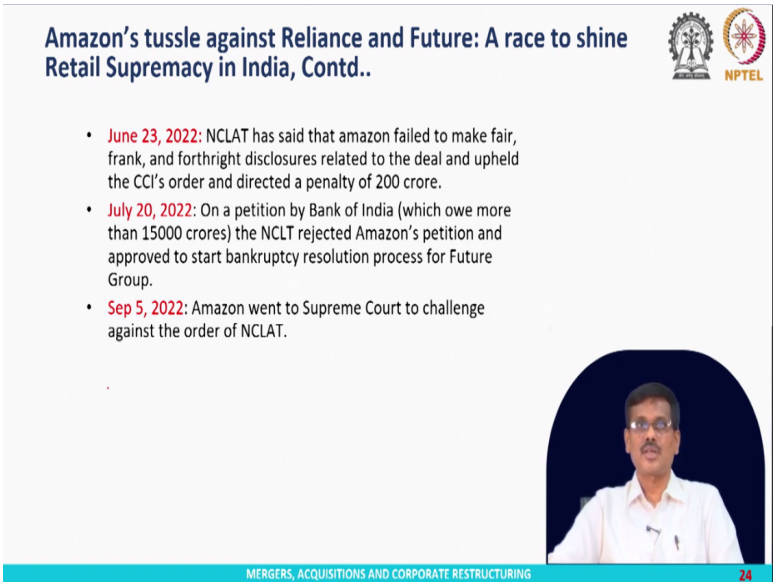

So, again it is not over and June 23rd NCLT appellate tribunal has said that Amazon has failed to make a fair and frank forthright disclosures about the deal. So, they upheld the CCI order and directly penalty of Rs. 200 crore to them to Amazon then Bank of India since consortium has applied for the insolvency. NCLT also rejected Amazon's petition and Amazon now has gone to Supreme Court to challenge the order of NCLT and we will see what is finally what the outcome is going to be for that matter.

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So, in this particular session we talked about different legal issues spanning different acts, regulations. We also talked about few points related to cross border acquisitions, what are the compliance procedures and typically in a cross border acquisition the compliance give us manifold as such and we also talked about the Reliance acquisition of future group and Amazon coming into picture all those things and similarly so acquisition acquiring company has to see that there may be diligent about the target company with respect to all legal aspects so that it can avoid the pitfalls in the future as such.

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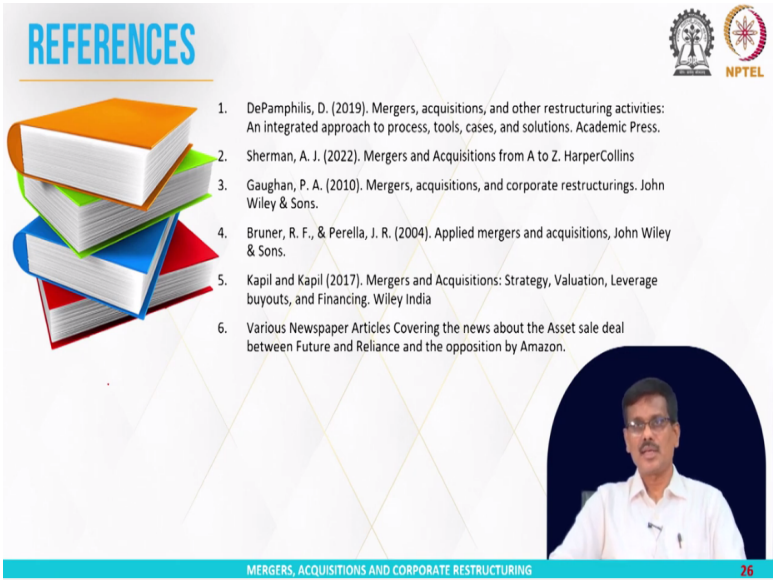

So, these are the references for that in the subsequent session we will take up a case of merger acquisition we will take up one case where a company has gone through multiple acquisition in certain time period and how the company has benefitted. So, thank you for this.