

# The Legal Side of Indian M&As

While a M&A is like any other commercial deal, there are many governing laws that must be understood in detail. **Manoj Kumar**, Assistant Vice President, Corporate Professionals Capital Private Limited explains the legal and people management aspects of an M&A



**M**&As are critical in corporate life and are considered as inevitable tools for inorganic growth. The main objective of a M&A is to add value to all the stakeholders, based on the assumption that it will produce higher corporate potential value than the value of the two separate entities. Trend shows that with economic prosperity, business houses tend to involve more and more in M&As to meet various corporate goals. Dynamics of India are strong and M&As have become a strategic choice for the growth of Indian companies. Many international and Indian M&As have helped companies to scale to the next pedestal and maximize the long-term value for stakeholders. However, practical experience shows that there are an equal number of cases where the M&As have failed to achieve the desired result.

Any major M&A transaction involves three major challenges – (1) commercial understanding including valuation & consideration (2) legal compliances to implement the transaction; and (3) post transaction implementation issues to achieve the desired advantages of a M&A.

## Commercial understanding

As business grows, the management feels the compulsion of inorganic growth – to go at an upper echelon, to create larger market share, to enter into new geographic horizons or a new line of business. Thus, the search for

M&A target starts, which leads to deal negotiations, business due diligence, valuations and arriving at commercial understanding for M&As. With the help of experts, a structure of the transaction is created to make it optimal in terms of cost, efforts and time.

## Legal compliance phase

While framing the deal structure, legal framework governing the transaction is very significant. The legal complexity of an M&A depends upon the nature of business, size of entities involved, geographical coverage of the businesses and mode of transaction finalized. The primary law governing M&As is the Indian Companies Law; however, there are several other statutes which directly or indirectly govern these transactions:

## QUICK VIEW

- The legal framework for M&A in India segregates Mergers from Acquisitions.
- Mergers refer to consolidation of two or more business entities in which any one or all entities lose their legal existence, whereas Acquisitions refer to the takeover of controlling stakes of one company by another

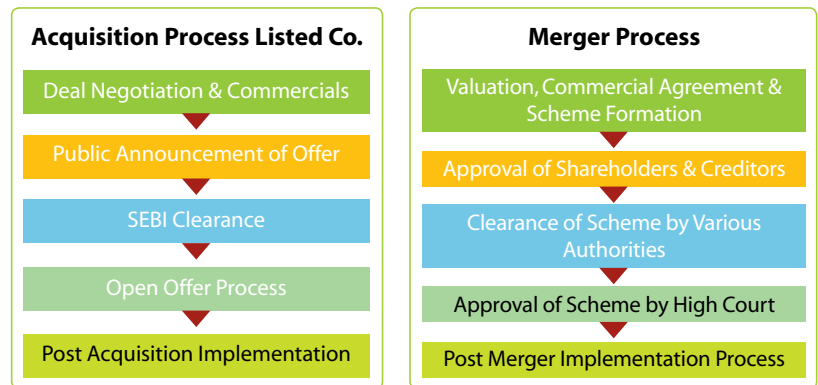
- The Tax Laws – basically Income Tax.
- Stamp duty & property tax provisions of respective states.
- Regulatory frameworks of the industry.
- Accounting norms as prescribed for M&A.
- In case of listed companies – Securities Laws especially SEBI Takeover Regulations & Listing Agreements with Stock Exchanges.
- Foreign Exchange Laws in case of cross-border M&A.
- Anti-trust laws or Competition Act if the size of businesses are significant.

The legal framework for M&A in India segregates Mergers from Acquisitions. Mergers refer to consolidation of two or more business entities in which any one or all entities lose their legal existence, whereas Acquisitions refer to the takeover of controlling stakes of one company by another. In this situation, the legal existence of the acquired entity continues.

In Acquisitions, involving Indian companies where none of the entities are listed, the process is much simpler in terms of legal compliances and here commercial considerations and cost aspects due to tax and stamp duties play a significant role. The transaction is carried through private agreements to cover commercial understanding.

Acquisition of an Indian Listed Company is mainly governed by the SEBI (Substantial Acquisition of Shares & Takeover) Regulations (also called 'SEBI Takeover Regulations'). These Regulations mandate an Open Offer by the Acquirer of a Listed Company to acquire at least 20% more stake in the Listed Company from the public shareholders at a price equal to or more than the price at which it acquires the substantial stake (15% or more). This provision is meant to give an exit opportunity to public shareholders who might not be interested to continue with the new management. Mergers (or amalgamations) of Indian companies are highly regulated and require various approvals – first by the BOD of the companies involved, then by the shareholders and creditors, then by Central Government (through Regional Director of Ministry of Corporate Affairs & Official Liquidator) and finally by the High Courts of the states where the registered offices are situated. Thus, the whole process takes 5-6 months. If the Merger involves one or more listed companies, then additionally, prior approval of the Stock Exchanges where the securities of the company are listed would be required.

Though Mergers or Acquisitions are just a commercial choice of structuring a deal, when it comes to cross-border M&As, the difference becomes significant as Indian law does not permit merger of an Indian company with a foreign



## M&A implementation needs to be carried out keeping in mind the **legal framework governing the transactions**

company and hence only inbound acquisitions are possible and mergers are not permissible.

### Post transaction implementation phase

Generally, for M&A deals, companies involve finance, taxation and legal team/experts and take due care of all commercial aspects - business, markets, financial, legal, etc.. But in most of the cases, HR issues like post M&A organizational design and cultural differences are often overlooked. Experience tells that HR plays a critical role in a successful M&A. Announcement of a M&A creates an uncertainty in the minds of employees with questions relating to job security, loss of identity and power status and adjustment to the cultural differences, etc. cropping-up, which need to be handled delicately. Lack of HR planning and communication may lead to suspicion, demoralization and loss of key personnel, which ultimately leads to loss of business. The HR issues are more behavioral than legal. The HR & Labor Laws in India do not cater to M&As and the same is broadly governed by the Transaction Agreement or Scheme of Merger and hence must be managed tactfully to make the transaction a success.

While M&A strategies originate from commercial considerations, its implementation needs to be carried out keeping in mind the legal framework governing these transactions, tax and other cost aspects, contractual obligations and impact of cultural and HR issues. Hence, it is important to craft an M&A deal in a very thoughtful manner so that maximum advantage can be derived with the least possible hassle. **PM**