



CRITICAL REVIEW ON MERGERS AND ACQUISITIONS: AN ESSENCE OF INDIAN SCENARIO

Mrs. A. Sarada* Mrs. P. Spoorthy Mr. B. Naveen Kumar*****

**Assistant Professor, Department of MBA, ST. Martins Engineering College, Hyderabad.*

***Assistant Professor, Department of MBA, CMR Campus, Medchal, Hyderabad.*

****Assistant Professor, Department of MBA, Bellary Institute of Technology and Management, Bellary, Karnataka.*

Abstract

The increased competition in the global market has prompted the Indian companies to go for mergers and acquisitions as an important strategic choice. The trends of mergers and acquisitions in India have changed over the years. The immediate effects of the mergers and acquisitions have also been diverse across the various sectors of the Indian economy. Till recent past, the incidence of Indian entrepreneurs acquiring foreign enterprises was not so common. The situation has undergone a sea change in the last couple of years. Acquisition of foreign companies by the Indian businesses has been the latest trend in the Indian corporate sector. The reason behind mergers and acquisitions (M&A) is that two companies together are more valuable than two separate companies. The key principle behind buying a company is to create shareholder value over and above that of the sum of the two companies. Indian markets have witnessed burgeoning trend in mergers which may be due to business consolidation by large industrial houses, consolidation of business by multinationals operating in India, increasing competition against imports and acquisition activities. Therefore, it is ripe time for business houses and corporate to watch the Indian market and grab the opportunity.

Introduction

The Indian economic reform since 1991 has opened up a whole lot of challenges both in the domestic and international spheres. The increased competition in the global market has prompted the Indian companies to go for mergers and acquisitions as an important strategic choice. The trends of mergers and acquisitions in India have changed over the years. The immediate effects of the mergers and acquisitions have also been diverse across the various sectors of the Indian economy. Till recent past, the incidence of Indian entrepreneurs acquiring foreign enterprises was not so common. The situation has undergone a sea change in the last couple of years. Acquisition of foreign companies by the Indian businesses has been the latest trend in the Indian corporate sector. The Indian IT and ITES sectors have already proved their potential in the global market. The other Indian sectors are also following the same trend. The increased participation of the Indian companies in the global corporate sector has further facilitated the merger and acquisition activities in India. The various factors that played their parts in facilitating the mergers and acquisitions in India are favorable government policies, buoyancy in economy, additional liquidity in the corporate sector, and dynamic attitudes of the Indian entrepreneurs are the key factors behind the changing trends of mergers and acquisitions in India.

The reason behind mergers and acquisitions (M&A) is that two companies together are more valuable than two separate companies. The key principle behind buying a company is to create shareholder value over and above that of the sum of the two companies. This rationale is particularly alluring to companies when times are tough. Strong companies will act to buy other companies to create a more competitive, cost- efficient company.

Comprehensive Overview on M&A

M&A have been a part of the business world for centuries. In today's dynamic economic environment, companies are often faced with decisions concerning these actions - after all, the job of management is to maximize shareholder value. Through mergers and acquisitions, a company can develop a competitive advantage and ultimately increase shareholder value. The said terms to a layman may seem alike but in legal/ corporate terminology, they can be distinguished from each other.

Merger: A full joining together of two previously separate corporations. A true merger in the legal sense occurs when both businesses dissolve and fold their assets and liabilities into a newly created third entity. This entails the creation of a new corporation.

Acquisition: Taking possession of another business also called a takeover or buyout. It may be share purchase (the buyer buys the shares of the target company from the shareholders of the target company. The buyer will take on the company with all its assets and liabilities.) or asset purchase (buyer buys the assets of the target company from the target company) In simple terms, A merger involves the mutual decision of two companies to combine and become one entity; it can be seen as a decision made by two "equals", whereas an acquisition or takeover on the other hand, is characterized the purchase of a smaller company by a much larger one. This combination of "unequal" can produce the same benefits as a merger, but it does not necessarily have to be a mutual decision. A typical merger, in other words, involves two relatively



equal companies, which combine to become one legal entity with the goal of producing a company that is worth more than the sum of its parts. In a merger of two corporations, the shareholders usually have their shares in the old company exchanged for an equal number of shares in the merged entity. In an acquisition, the acquiring firm usually offers a cash price per share to the target firm's shareholders or the acquiring firm's shares to the shareholders of the target firm according to a specified conversion ratio. Either way, the purchasing company essentially finances the purchase of the target company, buying it outright for its shareholders

Joint Venture: Two or more businesses joining together under a contractual agreement to conduct a specific business enterprise with both parties sharing profits and losses. The venture is for one specific project only, rather than for a continuing business relationship as in a strategic alliance.

Strategic Alliance: A partnership with another business in which you combine efforts in a business effort involving anything from getting a better price for goods by buying in bulk together to seeking business together with each of you providing part of the product. The basic idea behind alliances is to minimize risk while maximizing your leverage.

Partnership: A business in which two or more individuals who carry on a continuing business for profit as co-owners. Legally, a partnership is regarded as a group of individuals rather than as a single entity, although each of the partners file their share of the profits on their individual tax returns. Many mergers are in truth acquisitions. One business actually buys another and incorporates it into its own business model.

Basic Objectives of M&A

1. It will reduce the tax burden
2. It prevents exploitation of underutilisation of resources
3. It will increase profits
4. Optimum utilisation of all resources

Legal formalities behind M&A

Sections 390 to 394 of the Companies Act 1956 (the "Merger Provisions") and Section 230 to 234 of Companies Act 2013 (hereinafter referred to as CA) govern mergers and schemes of arrangements between a company, its shareholders. Since a merger essentially involves an arrangement between the merging companies and their respective shareholders, each of the companies proposing to merge with the other(s) must make an application to the Company Court having jurisdiction over such company for calling meetings of its respective shareholders and or creditors. The Court may then order a meeting of the creditors or shareholders of the company. If the majority in number representing 3/4th in value of the creditors and shareholders' present and voting at such meeting agrees to the merger, then the merger, if sanctioned by the Court, is binding on all creditors/shareholders of the company. Indian competition law grants a maximum time period of 210 days for the determination of the combination, which comprises acquisitions, mergers, amalgamations and the like. One needs to take note of the fact that this stated time frame is clearly distinct from the minimum compulsory wait period for applicants.

As per the law, the compulsory period of waiting for applicants can either be 210 days starting from the day of notice filing or receipt of the Commission's order, whichever occurs earlier. The threshold limits for firms entering business combinations are substantially high under the Indian law. The threshold limits are set either in terms of the asset value or in terms of the firm's turnover. Indian threshold limits are greater than those for the EU. They are twice as high when compared with UK.

The Indian law also provides for the modern day phenomenon of merger and acquisitions, which are cross border in nature. As per the law domestic nexus is a pre-requisite for notification on this type of combinations.

It can be noted that Competition Act, 2002 has undergone a recent amendment. This has replaced the voluntary notification regime with a mandatory regime. Of the total number of 106 countries, which possess competition laws only 9 are thought to be credited with a voluntary notification regime. Voluntary notification regimes are generally associated with business uncertainties. Post-combination, if firms are seen to be involved in anti-competitive practices de-merger shows the way out.

Provisions under Mergers and Acquisitions Laws in India

- Provision for tax allowances for mergers or de-mergers between two business identities is allocated under the Indian Income tax Act. To qualify the allocation, these mergers or de-mergers are required to fulfill the requirements related to section 2(19AA) and section 2(1B) of the Indian Income Tax Act as per the pertinent state of affairs.



- Under the “Indian I-T tax Act”, the firm, either Indian or foreign, qualifies for certain tax exemptions from the capital profits during the transfers of shares.
- In case of “foreign company mergers”, a situation where two foreign firms are merged and the new formed identity is owned by an Indian firm, a different set of guidelines are allotted. Hence the share allocation in the targeted foreign business identity would be acknowledged as a transfer and would be chargeable under the Indian tax law.
- As per the clauses mentioned under section 5(1) of the Indian Income Tax Act, the international earnings by an Indian firm would fall under the category of 'scope of income' for the Indian firm.

Motives behind M&A

These motives are considered to add shareholder value. This generally refers to a method in which the average cost per unit is decreased through increased production, since fixed costs are shared over an increased number of goods. In a layman’s language, more the products, more is the bargaining power. This is possible only when the companies merge/ combine/ acquired, as the same can often obliterate duplicate departments or operation, thereby lowering the cost of the company relative to theoretically the same revenue stream, thus increasing profit. A merger can also improve a company's standing in the investment community: bigger firms often have an easier time raising capital than smaller ones. The general advantage behind mergers and acquisition is that it provides a productive platform for the companies to grow, though much of it depends on the way the deal is implemented. It is a way to increase market penetration in a particular area with the help of an established base.

Conclusion

In real terms, the rationale behind mergers and acquisitions is that the two companies are more valuable, profitable than individual companies and that the shareholder value is also over and above that of the sum of the two companies. Despite negative studies and resistance from the economists, M&A’s continue to be an important tool behind growth of a company. Reason being, the expansion is not limited by internal resources, no drain on working capital - can use exchange of stocks, is attractive as tax benefit and above all can consolidate industry - increase firm's market power. With the FDI policies becoming more liberalized, Mergers, Acquisitions and alliance talks are heating up in India and are growing with an ever increasing cadence. Indian markets have witnessed burgeoning trend in mergers which may be due to business consolidation by large industrial houses, consolidation of business by multinationals operating in India, increasing competition against imports and acquisition activities. Therefore, it is ripe time for business houses and corporate to watch the Indian market and grab the opportunity.