

PROCEDURE FOR MERGER AND AMALGAMATION

ICAI-ARF GROUP



Procedure for merger and amalgamation is different from takeover. Mergers and amalgamations are regulated under the provisions of the Companies Act, 1956 whereas takeovers are regulated under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations.

The beginning to amalgamation may be made through common agreements between the transferor and the transferee but mere agreement does not provide a legal cover to the transaction unless it carries the sanction of company court for which the procedure laid down under section 391 of the Companies Act should be followed for giving effect to amalgamation through the statutory instrument of the court's sanction.

Although chapter V of the Companies Act, 1956 comprising

sections 389 to 396-A deals with the issue and related aspects covering arbitration, compromises, arrangements and reconstructions but at different times and under different circumstances in each case of merger and amalgamation application of other provisions of the Companies Act, 1956 and ruled made there-under may necessarily be attracted. So, the procedure does not remain simple or literally confined to chapter V.

The procedure is complex, involving not only the compromises or arrangements between the company and its creditors or any class of them or between the company and its members or any class of them but it involves, safeguard of public interest and adherence to public policy. These aspects are looked after by the Central Government through official liquidator on Company Law Board, Department of Company Affairs and the court has to be satisfied of the same.

Top management's commitments towards merger and amalgamation

Top management defines the

organisation's goal and outlines the policy framework to achieve these objectives. The organisation's goal for business expansion could be accomplished, *inter alia* through business combinations assimilating a target corporate which can remove the present deficiencies in the organization and can contribute in the required direction to accomplish the goal of business expansion through enhanced commercial activity i.e. supply of inputs and market for output product diversification, adding up new products and improved technological process, providing new distribution channels and market segments, making available technical personnel and experienced skilled manpower, research and development establishments etc. Depending upon the specific need and cost advantage with reference to creating a new set up or acquiring a well-established set-up firm.

Search for a merger partner

The top management may use their own contacts with competitors in the same line of economic activity or in the other diversified field which

could be identified as better merger partners or may use the contacts of merchant bankers, financial consultants and other agencies in locating suitable merger partners. A number of corporate candidates may be shortlisted and identified. Such identification should be based on the detailed information of the merger partners collected from published and private sources. Such information should reveal the following aspects viz:

- 1) Organisational history of business and promoters and capital structure
- 2) Organisational goals
- 3) Product, market and competitors
- 4) Organisational setup and management pattern
- 5) Assets profile: Movable and immovable assets, land and building
- 6) Manpower – skilled, unskilled, technical personnels and detailed particulars of management employees.

Negotiations

Top management can negotiate at a time with several identified shortlisted companies suited to be merger partner for settling terms of merger and pick up one of them which offers most favourable terms.

Negotiations can be had with target companies before making any acquisitional attempt. Samedrill of negotiations could be followed in the cases of merger and amalgamation.

Appendix II provides activity

schedule for planning merger covering different aspects like preliminary consultations with the prospective merger partner and seeking its willingness to cooperate in investigations. There are other aspects, too, in the activity schedule covering, quantification action plan, purpose, shape, and date of merger, profitability and valuation, taxation aspects legal aspects and development plan of the company after merger.

Steps for merger and amalgamation

Once the merger partner has been identified and terms of merger are settled the procedure summarized in Appendix III can be followed. An explanation to the said steps is given below:

1) Scheme of amalgamation

The scheme of amalgamation should be prepared by the companies, which have arrived at a consensus to merge. There is no specific form prescribed for scheme of amalgamation but scheme should generally contain the following information:

1. Particulars about transferee and transferor companies
2. Appointed date
3. Main terms of transfer of assets from transferor to transferee with power to execute on behalf or for transferee the deed or documents being given to transferee.
4. Main terms of transfer liabilities from transferor to transferee covering any conditions

attached to loans/debentures/bonds/other liabilities from bank /financial institution/trustees and listing conditions attached thereto.

5. Effective date when the scheme will come into effect
6. Conditions as to carrying on the business activities by transferor between 'appointed date' and 'effective date'.
7. Description of happenings and consequences of the scheme coming into effect on effective date.
8. Share capital of transferor company specifying authorized capital, issued capital and subscribed and paid up capital
9. Share capital of transferee company covering above heads.
- 10 Description of proposed share exchange ratio, any conditions attached thereto, any fractional share certificates to be issued, transferee company's responsibility to obtain consent of concerned authorities for issue and allotment of shares and listing.
- 11 Surrender of shares by shareholder of transferor company for exchange into new share certificates.
- 12 Conditions about payment of dividend, ranking of equity shares, pro rata dividend declaration and distribution.
- 13 Status of employees of the transferor companies from effective date and the status of the provident fund, gratuity fund, super annuity fund or any special scheme or funds cre-

ated or existing for the benefit of the employees.

14. Treatment on effective date of any debit balance of transferor company balance sheet.
15. Miscellaneous provisions covering income-tax dues, contingencies and other accounting entries deserving attention or treatment.
16. Commitment of transferor and transferee companies towards making applications/petitions under section 391 and 394 and other applicable provisions of the Companies Act, 1956 to their respective High Courts.
17. Enhancement of borrowing limits of the transferee company upon the scheme coming into effect.
18. Transferor and transferee companies give assent to change in the scheme by the court or other authorities under the law and exercising the powers on behalf of the companies by their respective Boards.
19. Description of powers of delegatee of transferee to give effect to the scheme.
20. Qualification attached to the scheme, which require approval of different agencies, etc.
21. Description of revocation/cancellation of the scheme in the absence of approvals qualified in clause 20 above not granted by concerned authorities.
22. Statement to bear costs etc. in connection with the scheme by the transferee company.

A specimen of the scheme is appended at the end of this chapter as Annexure 1.

(2) Approval of Board of Directors for the scheme

Respective Board of Directors for transferor and transferee companies are required to approve the scheme of amalgamation.

(3) Approval of the scheme by specialised financial institutions/banks/trustees for debenture holders

The Board of Directors should in fact approve the scheme only after it has been cleared by the financial institutions/banks, which have granted loans to these companies or the debenture trustees to avoid any major change in the meeting of creditors to be convened at the instance of the Company Court's under section 391 of the Companies Act, 1956.

Approval of Reserve Bank of India is also needed where the scheme of amalgamation contemplates issue of share/payment of cash to non-resident Indians or foreign national under the provisions of Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000.

In particular, regulation 7 of the above regulations provide for compliance of certain conditions in the case of scheme of merger or amalgamation as approved by the court.

(4) Intimation to Stock Exchange about proposed amalgamation

Listing agreements entered into between company and stock exchange require the company to communicate price-sensitive information to the stock exchange immediately and simultaneously

when released to press and other electronic media on conclusion of Board meeting according approval to the scheme.

(5) Application to Court for directions



The next step is to make an application under section 39(1) to the High Court having jurisdiction over the Registered Office of the company, and the transferee company should make separate applications to the High Court. The application shall be made by a Judge's summons in Form No. 33 supported by an affidavit in Form No. 34 (see rule 82 of the Companies (Court) rules, 1959). The following documents should be submitted with the Judge's summons:

- (a) A true copy of the Company's Memorandum and Articles
- (b) A true copy of the Company's latest audited balance sheet
- (c) A copy of the Board resolution, which authorises the Director to make the application to the High Court.

(6) High Court directions for members' meeting

Upon the hearing of the summons, the High Court shall give directions fixing the date, time and venue and quorum for the members'

meeting and appoint an Advocate Chairman to preside over the meeting and submit a report to the Court.

Similar directions are issued by the court for calling the meeting of creditors in case such a request has been made in the application.

(7) Approval of Registrar of High Court to notice for calling the meeting of members/creditors

Pursuant to the directions of the Court, the transferor as well as the transferee companies shall submit for approval to the Registrar of the respective High Courts the draft notices calling the meetings of the members in Form No. 36 together with a scheme of arrangements and explanations, statement under section 393 of the Companies Act and form of proxy in Form No. 37 of the Companies (Court) Rules to be sent members alongwith the said notice. Once Registrar has accorded approval to the notice, it should be got signed by the Chairman appointed for meeting by the High Court who shall preside over the proposed meeting of members.

(8) Despatch of notices to members/shareholders

Once the notice has been signed by the chairman of the forthcoming meeting as aforesaid it could be despatched to the members under certificate of posting at least 21 days before the date of meeting (Rule 73 of Companies (Court) Rules, 1959).

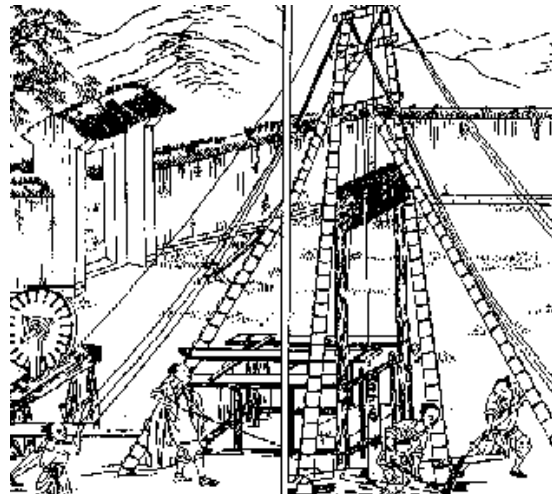
(9) Advertisement of the notice of members' meetings

The Court may direct the issuance of notice of the meeting of

these shareholders by advertisement. In such case rule 74 of the Companies (Court) Rules provides that the notice of the meeting should be advertised in; such newspaper and in such manner as the Court might direct not less than 21 clear days before the date fixed for the meeting. The advertisement shall be in Form No. 38 appended to the Companies (Court) Rules. The companies should submit the draft for the notice to be published in Form No. 38 in an English daily together with a translation thereof in the regional language to the Registrar of High Court for his approval. The advertisement should be released in the newspapers after the Registrar approves the draft.

(10) Confirmation about service of the notice

Ensure that at least one week



before the date of the meeting, the Chairman appointed for the meeting files an Affidavit to the Court about the service of notices to the shareholders that the directions regarding the issue of notices and advertisement have been duly complied with.

(11) Holding the shareholders'

general meeting and passing the resolutions

The general meeting should be held on the appointed date. Rule 77 of the Companies (Court) Rules prescribes that the decisions of the meeting held pursuant to the court order should be ascertained only by taking a poll. The amalgamation scheme should be approved by the members, by a majority in number of members present in person or on proxy and voting on the resolution and this majority must represent at least 3/4ths in value of the shares held by the members who vote in the poll.

(12) Filing of resolutions of general meeting with Registrar of Companies

Once the shareholders general meeting approves the amalgamation scheme by a majority in number of members holding not less than 3/4 in value of the equity shares, the scheme is binding on all the members of the company. A copy of the resolution passed by the shareholders approving the scheme of amalgamation should be filed with the Registrar of Companies in Form No. 23 appended to the Companies (Central Government's) General Rules and Forms, 1956 within 30 days from the date of passing the resolution.

(13) Submission of report of the chairman of the general meeting to Court

The chairman of the general meeting of the shareholders is required to submit to the Court

within seven days from the date of the meeting a report in Form No. 39, Companies (Court) Rules, 1959 setting out therein the number of persons who attend either personally or by proxy, and the percentage of shareholders who voted in favour of the scheme as well as the resolution passed by the meeting.

(14) Submission of Joint petition to court for sanctioning the scheme

Within seven days from the date on which the Chairman has submitted his report about the result of the meeting to the Court, both the companies should make a joint petition to the High Court for approving the scheme of amalgamation. This petition is to be made in Form No. 40 of Companies (Court) Rules. The Court will fix a date of hearing of the petition. The notice of the hearing should be advertised in the same papers in which the notice of the meeting was advertised or in such other newspapers as the Court may direct, not less than 10 days before the date fixed for the hearing (Rule 80 of Companies (Court) Rules].

(15) Issue of notice to Regional Director, Company Law Board under section 394 – A

On receipt of the petition for amalgamation under section 391 of Companies Act, 1956 the Court will give notice of the petition to the Regional Director, Company Law Board and will take into consideration the representations, if any, made by him.

(16) Hearing of petition and confirmation of scheme

Having taken up the petition by

the Court for hearing it will hear the objections first and if there is no objection to the amalgamation scheme from Regional Director or from any other person who is entitled to oppose the scheme, the Court may pass an order approving the scheme of amalgamation in; Form No. 41 or Form No. 42 of Companies (Court) Rules. The court may also pass order directing that all the property, rights and powers of the transferor company specified in the schedules annexed to the order be transferred without further act or deed to the transferee company and that all the liabilities and duties of the transferor company be transferred without further act or deed.

(17) Filing of Court order with ROC by both the companies

Both the transferor and transferee companies should obtain the Court's order sanctioning the scheme of amalgamation and file the same with ROC with their respective jurisdiction as required vide section 394(3) of the Companies Act, 1956 within 30 days after the date of the Court's order in Form No. 21 prescribed under the (Central Government's) General Rules and Forms, 1956. The amalgamation will be given effect to from the date on which the High Court's order is filed with the Registrar.

(18) Transfer of the assets and liabilities

Section 394(2) vests power in the High Court to order for the transfer of any property or liabilities from transferor company to transferee company. In pursuance of and by virtue of such order such properties and liabilities of the transferor shall automatically stand transferred to

transferee company without any further act or deed from the date the Court's order is filed with ROC.

(19) Allotment of shares to shareholders of transferor company

Pursuant to the sanctioned scheme of amalgamation, the shareholders of the transferor company are entitled to get shares in the transferee company in the exchange ratio provided under the said scheme. There are three different situations in which allotment could be given effect:

1. Where transferor company is not a listed company, the formalities prescribed under listing agreement do not exist and the allotment could take place without setting the record date or giving any advance notice to shareholders except asking them to surrender their old share certificates for exchange by the new ones.
2. The second situation will emerge different where transferor company is a listed company. In this case, the stock exchange is to be intimated of the record date by giving at least 42 days notice or such notice as provided in the listing agreement.
3. The third situation is where allotment to Non-Resident Indians is involved and permission of Reserve Bank of India is necessary. The allotment will take place only on receipt of RBI permission. In this connection refer to regulations 7, 9 and 10B of Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 as and where applicable.

Having made the allotment, the transferee company is required to file with ROC with return of allotment in Form No. 2 appended to the Companies (Central Government's) General Rules and Forms within 30 days from the date of allotment in terms of section 75 of the Act.

Transferee company shall having issued the new share certificates in lieu of and in exchange of old ones, surrendered by transferor's shareholders should make necessary entries in the register of members and index of members for the shares so allotted in terms of sections 150 and 151 respectively of the Companies Act, 1956.

(20) Listing of the shares at stock exchange

After the amalgamation is effected, the company which takes over the assets and liabilities of the transferor company should apply to the Stock Exchanges where its securities are listed, for listing the new shares allotted to the shareholders of the transferor company.

(21) Court order to be annexed to memorandum of transferee company

It is the mandatory requirement vide section 391(4) of the Companies Act, 1956 that after the certified copy of the Court's order sanctioning the scheme of amalgamation is filed with Registrar, it should be annexed to every copy of the Memorandum issued by the transferee company. Failure to comply with requirement renders the company and its officers liable to punishment.

(22) Preservation of books and papers of amalgamated Co.

Section 396A of the Act requires that the books and papers of the amalgamated company should be preserved and not be disposed of without prior permission of the Central Government.

(23) The Post merger secretarial obligations

There are various formalities to be complied with after amalgamation of the companies is given effect to and allotment of shares to the shareholders of the transferor company is over. These formalities include filing of returns with Registrar of Companies, transfer of investments of transferor company in; the name of the transferee, intimating banks and financial institutions, creditors and debtors about the transfer of the transferor company's assets and liabilities in the name of the transferee company, etc. All these aspects along with restructuring of organization and management and capital are discussed in chapter relating to post-merger reorganization of transferee company.

(24) Withdrawal of the Scheme not permissible

Once the scheme for merger has been approved by requisite majority of shareholders and creditors, the scheme cannot be withdrawn by subsequent meeting of shareholders by passing Resolution for withdrawal of the petition submitted to the court under section 391 for sanctioning the scheme.

(25) Cancellation of the scheme and order of winding-up

It was held by the Supreme Court in *J.K (Bombay) (P) Ltd. Vs. New Kaiser-I-Hind* that the effect of winding up order is that except for certain preferential payments provided in

the Act, the property of the company is applied in satisfaction of its liabilities *pari passu*. *Pari passu* distribution is to be made in satisfaction of its liabilities as they exist at the commencement of the winding-up.

So long as the scheme is in operation and is bind on the company and its creditors, the rights and obligations of those on whom it is binding are undoubtedly governed by its provisions. But once the scheme is cancelled under section 392(2) on the ground that it cannot be satisfactorily worked and a winding-up order passed such an order is deemed to be for all purposes to be one made under section 433. It is not because as if the scheme has been sanctioned under section 391 that a winding-up order under section 392 (2) cannot be made.

The Specialised formalities to cover up amalgamation

The steps for merger or amalgamation discussed above are not the only considerations effecting merger but in addition to the above and in relation thereto a number of special formalities are also complied with which have been covered in detail in specific chapters like share valuation and exchange ratio, accounting aspects of funding of reorganization plans, etc. These aspects have been given treatment under different chapters. Readers may refer to relevant chapters in the matter of drafting the scheme of amalgamation, carrying out valuation of the assets of the companies, calculating share exchange ratio, etc. wherever felt necessary. Case studies provided in the book are based on real happenings and provide practical insight into the procedural aspects. ■

A CHECKLIST FOR MERGERS & AMALGAMATION

Even as the wave of takeovers and mergers continues, any detailed studies and analysis are yet to arrive. However, some quick lessons can be drawn from the recent acquisitions:

Willing Co-operation of the Employees and their Unions:

The rough weather faced by the TOMCO-HLL merger has emphasised the need to take the employees and their unions into confidence. If the employees do not willingly support the merger/takeover, it may lead to legal battles.

Role of financial institutions and banks:

In countries such as Japan and Germany, the managements enter into alliances with their financial institutions and banks so as to gain control of companies.

The banks in India have been increasing investment banking activity and the relaxations by the RBI have facilitated this process. Besides this, the mutual funds and venture capital funds have also become major stakeholders in the public limited companies. By supporting competent management and removing inefficient ones, these institutions and banks can safeguard their investments and ensure proper returns.

Changing role of FIs – Need to be proactive

FIs cannot afford to remain silent in the current wave of takeovers. A more proactive approach is called for on their part. And considering that both FIs and banks held in building the saving system and that FIs own huge chunks of equity in most Indian companies, their role ought to become even more dynamic. A new kind of commercial prowess is required on their part and profit motive should become their goal.

The UTI, LIC and FIs represent small savers, policy-holders and shareholders respectively. The question as to whom they should support in the eventuality of a takeover should no longer be a difficult one. It should be guided by the principle of maximizing shareholder returns rather than paying the devil its due.

Increasing scope for merchant banking activity

Mergers and takeovers have also become a lucrative source of business for the merchant bankers. They are guiding their clients in various areas such as identification of industrial units which are suffering due to managerial deficiencies, paucity of funds etc. providing expertise in working out takeover or merger schemes deciding the share exchange ratio, seeking various clearances, proper implementations of merger or takeover schemes etc.

M&A although considered desirable to bring about competitive efficiency in the Indian economy, may prove counter productive if encouraged beyond a certain point. Managements apprehensive of corporate raiders may try to maximize short-term profits and pay higher dividends so as to keep the shareholders happy. This may happen at the cost of the long-term interests of the companies.

Choosing to modernize your factory instead of increasing your dividend might make shrewd business sense, but it is also a luring way to draw raiders. The moral is that because of all the bad mergers, good mergers are becoming impossible. Companies are paranoid today and you can't blame them. Chief executive officers are trying to plan ahead while looking over their shoulders.