Process of M&A Transactions

Lesson 4

KEY CONCEPTS

■ Due Diligence ■ Registered Valuer ■ Differential Pricing ■ Valuation ■ Regulatory Framework for Merger/ Amalgamation

Learning Objectives

To understand:

- Process of Merger & Acquisition
- Prerequisites of Merger & Acquisition
- Due Diligence
- Type of Due Diligence
- Due Diligence Check-List
- Factors Influencing valuation
- Regulatory Framework for Merger/Amalgamation

Lesson Outline

- Approvals in a Scheme of Merger & Amalgamation
- Steps involved in Merger
- Due Diligence
- Types of Due Diligence
- Practical Guide to the Due Diligence
- Factors Influencing Valuation
- Valuation Approach
- Integration of Business & Operations
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings

REGULATORY FRAMEWORK

- Companies Act, 2013
- The Companies (Compromises, Arrangements and Amalgamations) Rules, 2016
- The National Company Law Tribunal Rules, 2016

MERGER AND ACQUISITION

Process of Merger & Acquisition involves corporate control, strategy, corporate finance and management. It involves consolidation of companies i.e. business combination, division and demerger of two or more companies. The merger and amalgamation requires various regulatory approvals and procedures as enunciated in the Companies Act, 2013.

Merger being a strategy, it has to be object oriented and it dwells upon the concept of synergy, which means value of two companies together will be more than of an individual company. Merger & Acquisition could be by way of business purchase/share purchase agreement or by way of sanction of Scheme of Arrangement through the court route.

In a sense, in the case of merger through a court route, once the scheme is sanctioned by the court/tribunal after due process of law and the scheme is filed with the Registrar of Companies, it is irreversible; it carries the stamp of final approval by a judicial authority and is acceptable to the public, shareholders, stakeholders, registering authority.

Merger & Acquisition process is normally proceeded by formulation of strategy, identification of cost benefit analysis, carrying out due diligence, conducting valuation and considering the aspects of stamp duty and other applications. Moreover, the integration issue after the merger exercise is also to be taken care of.

Prerequisites of Merger and Acquisition

1. **Due Diligence**: It refers to the investigating effort made to gather all relevant facts and information that can influence a decision to enter into a transaction or not. Exercising due diligence is not a privilege but an unsaid duty of every party to the transaction. For instance, while purchasing a food item, a buyer must act with due diligence by checking the expiry date, the price, the packaging condition, etc. before paying for the product. It is not the duty of the seller to ask every buyer every time to check the necessary details. M&A due diligence helps to avoid legal hassles due to insufficient knowledge of important information.
2. **Business Valuation:** Business valuation or assessment is the first step of merger and acquisition. This step includes examination and evaluation of both the present and future market value of the target company. A thorough research is done on the history of the company with regards to capital gains, organizational structure, market share, distribution channel, corporate culture, specific business strengths, and credibility in the market. There are many other aspects that should be considered to ensure if a proposed company is right or not for a successful merger.
3. **Planning Exit**: When a company decides to sell its operations, it has to undergo the stage of exit planning. The company has to take firm decision as to when and how to make the exit in an organized and profitable manner. In the process the management has to evaluate all financial and other business issues like taking a decision of full sale or partial sale along with evaluating on various options of reinvestments.
4. **Structuring Business Deal**: After finalizing the merger and the exit plans, the new entity or the take-over company or target company has to take initiatives for marketing and creating innovative

strategies to enhance business and its credibility. The entire phase emphasize on structuring of the business deal.

5. **Stage of Integration**: This stage includes both the company coming together with their own parameters. It includes the entire process of preparing the document, signing the agreement, and negotiating the deal. It also defines the parameters of the future relationship between the two.

Some of key highlights of Companies Act, 2013 impacting merger and amalgamation

- Creation of treasury shares i.e. holding the share in its own name or in the name of the trust, whether on its own behalf or on behalf of any of its subsidiary or associated company is no longer permissible.
- Objections to the scheme can be raised only by shareholders holding at least 10% stake or creditors holding at least 5% of total outstanding debts as per the latest audited financial statements thereby avoiding unnecessary delays.
- Regulators to make representation within 30 days regarding scheme, else deemed 'no objections' or no representation on the proposal of such merger/amalgamation.
- No approval of Tribunal is required in case of merger between holding company and its 100% subsidiary or merger between small companies (based on prescribed capital/turnover).
- Merger of Indian company with foreign company located in certain jurisdictions is allowed subject to RBI Regulations/FDI Guidelines.
- Shareholders would have an option to vote for the scheme through postal ballot, e-voting in addition to voting physically at a meeting.

DUE DILIGENCE

Diligence: It means prudence; vigilant activity; attentiveness; or care, of which there are infinite shades, from the slightest momentary thought to the most vigilant anxiety. *People v. Hewitt, 78 Cal. App. 426, 248 P. 1021, 1024*1.

Due diligence: Such a measure of prudence, activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent man under the particular circumstances; not measured by any absolute standard, but depending on the relative facts of the special case. *Perry v. Cedar Falls*, *87 Iowa, 315, 54 N.W. 225*.

Due diligence is an investigation of a business or person prior to signing a contract, or an act with a certain standard of care. It can be a legal obligation, but the term will more commonly apply to voluntary investigations. A common example of due diligence in various industries is the process through which a potential acquirer/ investor evaluates a target company including its assets for an acquisition. The theory behind due diligence holds that performing this type of investigation contributes significantly to informed decision making by enhancing the amount and quality of information available to decision makers and by ensuring that this information is systematically used to deliberate in a reflexive manner on the decision at hand and all its costs, benefits, and risks.

Due diligence is integral to business. It is exercised in a simple over-the-counter transaction or a complicated merger and acquisition transaction. For instance, while acquiring a company, the buyer must do thorough research of the credentials of the company, its market valuation, status of accounts receivables, product and brand involved, position in the debt market, status of legal and statutory compliances, past performance, etc. It is also essential to study the previous financial reports to analyze the company's performance, to check the company background, its promoters, general reputation, and return to the existing shareholders.

Thus, a due diligence is an investigation or audit of a potential investment. It seeks to confirm all material facts in regard to a sale. It is a way of preventing unnecessary harm/hassles to either party involved in a transaction. It first came into use as a result of the US Securities Act, 1933.

TYPES OF DUE DILIGENCE

The different types of Due Diligence may be as follows:

Legal Due Diligence: Legal Due Diligence is used to ensure that there are no legal issues in buying a business or investing in it. In this, the potential purchaser will review the important legal documents of the target firm such as employment contracts, board meeting minutes, articles and memorandum of association and patents and copyrights or any other property related documents compliance status of the applicable laws etc.

Tax Due Diligence: This is aimed at ensuring that there are no past tax liabilities in the seller firm that might have materialized due to mistakes or deception and could hold the acquirer liable for it.

IP Due Diligence: IP due diligence is focused on establishing what rights the company may have in various intellectual property and where it might rely on the intellectual property of another entity. Typical areas of interest are patent, copyright and trademark filings; descriptions of the company's IP protection processes; licensing agreements, IP Assignment document, etc.

Operational Due Diligence: Operational due diligence (ODD) is the process by which a potential purchaser reviews the operational aspects of a target company during mergers and acquisitions. The ODD review looks at the main operations of the target company and attempts to confirm (or not) that the business plan that has been provided is achievable with the existing operational facilities plus the capital expenditure that is outlined in the business plan.

Commercial Due Diligence: This aims at understanding the market the target business is operating in. This looks the current market status and the forecast of the market growth in future and the target's position in the market with relation to its competitors. This also involves interaction with the significant customers of the business to understand their opinion about the business.

Information Technology (IT) Due Diligence: This aims at identifying if there are any IT issues in the target business. This involves into matters such as scalability of systems, robustness of the processes, availability of ERP, IT base and infrastructure, capacity of server, the level of documentation of processes, compliance with the legislation and ability to integrate various systems.

HR Due Diligence: This aims at understanding the impact of human capital on the proposed deal. This involves review of number and type of manpower, skills, employment records, compensation schemes, HR processes, ongoing HR litigations, effectiveness of the sales force and cultural factors.

PRACTICAL GUIDE TO DUE DILIGENCE

Due diligence is a meaningful analysis of the collected information to arrive at some decision about the potential transaction. The due diligence exercise is a crucial task. In this process the financial and non-financial information of the target company is to be collected and analysed in order to derive profitability after acquiring the target company.

A successful due diligence depends to a large extent on the cooperation of the proposed seller. This is possible in the case of 'friendly' takeovers. Generally the buyer conducts a preliminary review of the target and after a 'provisional' offer is made by the buyer to denote interest in the acquisition, an environment is created for the target to allow access to the documents, records and most aspects of the business including the physical inspection of the undertaking.

The collection of the information relating to the target company is not an easy task specifically when the target company does not cooperate in the matter. The information may be gathered from the external as well as internal sources. External sources are available and can be extracted from the public domain; however gathering of the internal information is somewhat difficult.

Normally the due diligence process should incorporate the following areas, in order to assess the nitty-gritty of the transactions of the takeover and to opt for or opt out of the takeover deal:

1. **Industry Analysis**
   - Competition
   - Growth Rate
   - Future projections
   - Barriers to entry / exit
   - Mergers and acquisitions in industry and results
   - Brand evaluation.
2. **Management Analysis**
   - Company's HR Policies
   - Assessment of Senior Level Management, resumes of key employees their qualifications and work exposures, previous background, etc.
   - Summary Plan descriptions of qualified and non-qualified retirement plans
   - Business Experience
   - Union Contract, copies of collective bargaining agreements, description of all employees problems within last five years including the alleged wrongful termination, harassment discrimination, etc.
   - Strike History
   - Labour Relations/ Agreements, grievance procedures, labour disputes currently pending or settled within last five years.
   - Workman's' compensation claim history / unemployment claim history
   - Personnel Schemes, description of benefits of all employees' health and welfare insurance policies
   - Profile of permanent employees
   - Labour dues and settlement history
   - Status of labour law compliances.
3. **Financial Analysis**
   - Audited Financial Statements along with auditor's reports for at least past five years or since inception.
   - Auditor s letters and replies for the past five years or since inception
   - The most recent unaudited statements, with comparable statements to the prior year.
   - The company's credit report, if available
   - Analyst reports, if available
   - Budgets and forecasts and strategic plans
   - Significant ratio analysis
   - Revenue versus cost comparison.

- A description of depreciation and amortization methods and changes in accounting methods since inception Schedules of:
  - All indebtedness and contingent liabilities
  - Stock
  - Accounts receivable
  - Non-current investment
  - Cash in hand/Cash Equivalent
  - Type of ownership rights
  - Tax Liabilities
  - Accounts payable
  - Fixed Assets and its locations (including the land holdings, real estate leases, deeds, mortgages, titled deeds etc)
  - All leases of equipment
  - Sale and purchases of major capital equipments made during the last five years.
- Financial ratios
  - Return on Assets
  - Return on Net worth
  - Gross Profit to Net Profit Ratio
  - Debt Equity Ratio
  - Expense Ratio
  - Debt-Service Coverage Ratio.
- Analysis of
  - Fixed and variable expenses
  - Gross margins
- The company's general ledger
- Replacement cost data
- Valuation of Assets / Liabilities
- A description of the company's internal control procedures
- Internal audit/control reports for last five years
- Insurance coverage of all assets.

4. Intellectual Property Rights

- A list of domestic and foreign patents and patent applications
- A list of trademark and trade names
- A list of copyrights

- A description of important technical know-how
- A description of methods used to protect trade secrets and know-how
- Any work for hire agreements
- A list of and copies of all consulting agreements, agreements regarding inventions, licences, or assignments of intellectual property to or from the company
- Any patent clearance documents
- A list of and summary of any claims or threatened claims by or against the company regarding intellectual property.

5. Taxes

- Income-tax returns for the last five year or since inception
- States sales/VAT returns /GST returns
- Assessment orders
- Tax audit, where applicable
- Any tax settlement documents
- Other tax filing statements (State and Central Excise).
- Number of current tax litigations, if any.

6. Marketing Analysis

- Data on Past Sales and future trend
- Customer base and profile
- Major sales agreements, warranty agreements, distributorship/franchisee agreements, product development agreements.
- Trends
- Distribution channels
- Product Profile
- Development / Disclosure.

7. Manufacturing

- Location
- Technology
- Manufacturing process
- Quality
- Research & Development
- Sourcing of Raw Material.

8. Compliance Status of various laws as applicable

- Companies Act 2013

- Stock Exchange Compliances, SEBI/RBI Regulations
- Labour Laws
- Competition laws
- Environmental Protection laws.

9. Litigation

- A schedule of all pending litigations
- A description of any threatened litigations
- Copies of insurance policies providing coverage as to pending or threatened litigation
- Documents relating to any injunctions, consent decrees, or settlements to which the company is a party
- A list of unsatisfied judgments.

MANAGING THE DUE DILIGENCE PROCESS

As due diligence is wholesome exercise that require specialized knowledge, expertise & experience to complete the task in time bound & effective manner, therefore during the due diligence process the following points are worth consideration:

- Constitute a due diligence team comprising of technical, legal, financial and taxation experts, etc.
- Assign the task to each of the member and the co-ordination among the members be supervised by a senior level officer.
- Collect the data of the target company with reference to the:
  - Corporate records
  - Promoter's holding
  - Stockholder information
  - Important contracts including IP, Sales, Purchase, IT, etc.
  - Compliance record
  - HR record
  - Finance record including access of softwares/ERP, etc.
  - History of litigation
  - Insurance information
  - Financials and leases.
- Analyse the above information/ statistics, assess the future prospects and the benefit in acquiring with reference to the market size and cutting of the competition.
- If the proposal, found feasible, follow the regulatory requirements as mentioned in the Companies Act, 2013 and the SEBI Regulations, RBI regulations, FDI guidelines & competition laws as applicable.

CONTENTS OF THE DUE DILIGENCE REPORT

The contents of a due diligence report should more or less include certain points which would draw the attention of the intending buyer, viz:

- Comments on the management and organisation,

- Details of key managerial/ technical personnel,
- Details of marketing efforts undertaken,
- Details of financial liabilities and commitments that the intending buyer would have to meet after takeover and which are not disclosed in the audited accounts,
- Deviations from the generally accepted accounting policies/ practices,
- Analysis of major expenditure/costs, details of major/critical customers and suppliers,
- Compliance of taxation and other statutory laws as well as status and impact of all litigation in this respect,
- Benefits enjoyed by the intending seller which the intending buyer may lose on takeover and vice versa,
- List of adjustments to the latest financial statements compiled on the basis of all findings, which have an impact on the "price" of the target acquisition to be considered by the intending buyer.
- Number and type of litigations,
- Details of key assets and customers takeaways.

DUE DILIGENCE CHECK-LIST

The acquiring company is always interested in the financial aspects, human aspects, assets and liabilities of the target company. The following due diligence checks may help in carrying out the process:

Financial Aspects:

- Read the auditor's report and qualifying remarks, if any and director's responsibility statement.
- Whether the company is profit making, dividend paying company
- Calculate financial ratios and compare it with the previous year(s) figures of the company and also compare with the industry trend.
- Whether the Balance sheet have any fictitious assets?
- Whether any assets have been re-valued (particularly of real estates) in current year or in past.
- Calculate Net worth and its components and compare it with the previous year(s) figures.
- Compare the cash flow statements of current year with that of the previous year(s).
- Whether the borrowing from banks/FI is classified as Standard Assets in the books of the bank.
- Whether clear demarcation is made between the capital and revenue income and expenditure.
- Whether any penalty from Revenue Authorities, Stock Exchanges/ SEBI/ CCI/ FEMA levied in the current / past years?
- Whether any litigation against the company, is pending before any court of law?
- Amount of contingent liabilities.

Debtor's Aspects:

- Study the demographic profile of the customer.
- Study the type of customer base.
- Whether sales are made in concentration / very few buyers are available in the market.

- What is the debt realisation cycle?
- What are the terms and conditions for sales on credit?
- How the sales campaign is made in order to lead the others in the market.

Creditor's Aspects:

- Who are the suppliers?
- What are the terms and conditions for purchase on credit?
- Whether the supplier is unique or discattered or no single supplier can mis-match the supply?

Material Control Aspect:

- Make a review of all material contracts and commitments of the target company.
- Study various issues pertaining to guaranties, loans, and credit agreements.
- Study the Customer and supplier contracts, Equipment leases, Indemnification agreements, License agreements, Franchise agreements, Equity finance agreements, Distribution, dealer, sales agency, or advertising agreements, Non-competition agreements, Union contracts and collective bargaining agreements, Contracts the termination of which would result in a material adverse effect on the company.

Human Aspect:

- Study the organization chart and biographical information,
- Type of workforce and expertise involved.
- Summary of any labour disputes, information concerning any previous, pending, or threatened labour stoppage,
- Employment and consulting agreements, loan agreements, and documents relating to other transactions with officers, directors, key employees, and related parties,
- Schedule of compensation paid to officers, directors, and key employees for the three most recent fiscal years showing separately salary, bonuses, and non-cash compensation (e.g., use of cars, property, etc.)
- Employee benefits and copies of any pension, profit sharing, deferred compensation, and retirement plans, management incentive or bonus plans not included in above as well as other forms of non- cash compensation, Employment manuals and policies, involvement of key employees and officers in criminal proceedings or significant civil litigation, Actuarial reports for past three years for gratuity valuations.

Regulatory Aspects:

- Study the revenue returns filed by the company and its assessment orders.
- Whether any penalty has been imposed for contraventions of the provisions of the law and such penalty is still due.
- Whether the company is abiding with the company law compliances. Check the various returns filed with the RoC.
- Is there any specific laws applicable and compliance of such laws are regular.

REGULATORY FRAMEWORK FOR MERGER/ AMALGAMATION

The Companies Act, 2013 has brought many enabling provisions with regard to mergers, compromise or arrangements, especially with respect to cross border mergers, time bound and single window clearances, enhanced disclosures, disclosures to various regulators, simplified procedure for smaller companies, etc.

The Regulatory framework of Mergers and Amalgamations covers:

1. The Companies Act, 2013
2. National Company Law Tribunal Rules, 2016
3. Companies (Compromise, Arrangements and Amalgamations) Rules, 2016
4. Income Tax Act, 1961
5. SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015
6. Competition Act, 2002
7. Approval from industry specific regulators, wherever required.

1. Companies Act, 2013

Chapter XV of Companies Act, 2013 comprising Sections 230 to 240 contains provisions on Compromises, Arrangements and Amalgamations. The scheme of Chapter XV is as follows:

1. Section 230-231 deals with compromise or arrangements with creditors and members and power of the Tribunal to enforce such a compromise or arrangement.
2. Section 232 deals with mergers and amalgamation including demergers.
3. Section 233 is relating to the merger or amalgamation of small companies or between the holding company and its wholly owned subsidiary (also called fast track mergers)
4. Section 234 deals with amalgamation with foreign company (also called cross border mergers).
5. Section 235 deals with acquisition of shares of dissenting shareholders.
6. Section 236 deals with purchase of minority shareholding.
7. Section 237 contains provisions as to the power of the Central Government to provide for amalgamation of companies in public interest.
8. Section 238 deals with registration of offer of schemes involving transfer of shares.
9. Section 239 deals with preservation of books and papers of amalgamated companies.
10. Section 240 deals with liability of officers in respect of offences committed prior to merger, amalgamation, etc.

2. Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 (read with National Company Law Tribunal Rules, 2016)

Rules 3 to Rule 29 contain provisions dealing with the procedure for carrying out a scheme of compromise or arrangement including amalgamation or reconstruction.

3. Income Tax Act, 1961

The Income Tax Act, 1961 covers aspects such as tax relief to amalgamating/amalgamated companies, carry forward of losses, exemptions from capital gains tax, etc. For example, when a scheme of merger or demerger involves the merger of a loss making company or a hiving-off of a loss making division, it is necessary to check the relevant provisions of the Income Tax Act and the Rules for the purpose of ensuring, *inter alia* , the availability of the benefit of carrying forward the accumulated losses and setting of such losses against the profits of the Transferor Company.

4. SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015

SEBI has notified SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations) on September 2, 2015. Companies are required to comply with the following:

— Scheme of Arrangement (Regulation11)

— Draft scheme of arrangement & scheme of arrangement (Regulation 37)

— Minimum Public Shareholding (Regulation 38)

For details please refer to Chapter 10 of this Study.

5. Indian Stamp Act, 1899

It is necessary to refer to the Indian Stamp Act, 1899 to check the stamp duty payable on transfer of undertaking through a merger or demerger.

6. Competition Act, 2002

The provisions of Competition Act, 2002 and the Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011 are to be complied with.

Provisions of the Companies Act, 2013

Chapter XV, comprising of sections 230 to 240 read with the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016, deals with Compromises, Arrangements and Amalgamations. The relevant details are explained below:

Section 230 - Power to compromise or make arrangements with creditors and members

Section 230 lays down in detail the power of a company to make compromise or arrangements with its creditors and members. Under this section, a company can enter in to a compromise or arrangement with its creditors or its members, or any class thereof.

Scope of Section 230

Section 230 deals with the rights of a company to enter into a compromise or arrangement (i) between itself and its creditors or any class of them; and (ii) between itself and its members or any class of them. The arrangement contemplated by the section includes a re-organisation of the share capital of a company by consolidation of its shares of different classes or by sub-division of its shares into shares of different classes or by both these methods.

The section also applies to compromise or arrangement entered into by companies under winding-up. Therefore, an arrangement under this section can take a company out of winding-up.

Sub-section (1)–Application to the Tribunal for convening meetings of members/creditors

Where a company or a creditor or a member of the company proposes a compromise or arrangement between it and its creditors or between it and its members or with any class of the creditors or any class of members, the company or the creditor or member, or where the company is being wound-up, the liquidator may make an application to the Tribunal. On such application, the Tribunal may order a meeting of the creditors or members or any class of them as the case may be and such meetings shall be called, held and conducted in such manner as the Tribunal may direct.

The key words and expressions under sub-section are ‘creditors’, ‘Tribunal’, ‘class of creditors or members’, ‘a company which is being wound-up’, ‘liquidator’. When a company is ordered to be wound-up, the liquidator is appointed and once winding-up commences liquidator takes charge of the company in all respects and therefore it is he who could file any application of any compromise or arrangement in the case of a company which is being wound-up. A company which is being wound-up would mean a company in respect of which the court has passed the winding-up order.

Sub-section (2)– Disclosures to the Tribunal by applicant under sub-section 1

Sub-section (2) provides that the company or any other person, who makes an application as provided under

sub-section (1) shall disclose by affidavit to the Tribunal:

(a) all material facts relating to the company, such as the latest financial position of the company, the latest auditor's report on the accounts of the company and the pendency of any investigation orproceedings against the company;

(b) reduction of share capital of the company, if any, included in the compromise or arrangement;

(c) any scheme of corporate debt restructuring consented to by not less than seventy-five percent of the secured creditors in value, including—

(i) a creditor's responsibility statement in the prescribed form;

(ii) safeguards for the protection of other secured and unsecured creditors;

(iii) report by the auditor that the fund requirements of the company after the corporate debt restructuring as approved shall conform to the liquidity test based upon the estimates provided to them by the Board;

(iv) where the company proposes to adopt the corporate debt restructuring guidelines specified by the Reserve Bank of India, a statement to that effect; and

(v) a valuation report in respect of the shares and the property and all assets, tangible and intangible, movable and immovable, of the company by a registered valuer.

Sub-section (3) – Notice of the meeting

Notice of the meeting called in pursuance of the order of the tribunal shall be sent to all the creditors or class of creditors and to all the members or class of members and the debenture-holders of the company, individually at the address registered with the company which shall be accompanied by

1. a statement disclosing the details of the compromise or arrangement,
2. a copy of the valuation report, if any, and
3. explaining their effect on creditors, key managerial personnel, promoters and non-promoter members, and the debenture holders and
4. the effect of the compromise or arrangement on any material interests of the directors of the company or the debenture trustees, and
5. such other matters as may be prescribed:

Such notice and other documents shall also be placed on the website of the company, if any, and in case of a listed company, these documents shall be sent to the Securities and Exchange Board and stock exchange where the securities of the companies are listed, for placing on their website and shall also be published in newspapers in such manner as may be prescribed: When the notice for the meeting is also issued by way of an advertisement, it shall indicate the time within which copies of the compromise or arrangement shall be made available to the concerned persons free of charge from the registered office of the company.

Sub-section (4) – Notice to provide for voting by themselves or through proxy or through postal ballot

Sub-section (4) states that a notice under sub-section(3) shall provide that the persons to whom the notice is sent may vote in the meeting either themselves or through proxies or by postal ballot to the adoption of the compromise or arrangement within one month from the date of receipt of such notice.

Provided that any objection to the compromise or arrangement shall be made only by persons holding not less than ten per cent. of the shareholding or having outstanding debt amounting to not less than five per cent of the total outstanding debt as per the latest audited financial statement.

Sub-section (5) – Notice to be sent to the regulators seeking their representations

Section 230 (5) states that a notice under sub-section (3) along with all the documents in such form as may be prescribed shall also be sent to the Central Government, the income-tax authorities, the Reserve Bank of India, the Securities and Exchange Board, the Registrar, the respective stock exchanges, the Official Liquidator, the Competition Commission of India established under sub-section (1) of section 7 of the Competition Act, 2002, if necessary, and such other sectoral regulators or authorities which are likely to be affected by the compromise or arrangement and shall require that representations, if any, to be made by them shall be made within a period of thirty days from the date of receipt of such notice, failing which, it shall be presumed that they have no representations to make on the proposals.

Sub-section (6): Approval and sanction of the scheme

Section 230 (6) states that when at a meeting held in pursuance of sub-section (1), majority of persons representing three-fourths in value of the creditors, or class of creditors or members or class of members, as the case may be, voting in person or by proxy or by postal ballot, agree to any compromise or arrangement and if such compromise or arrangement is sanctioned by the Tribunal by an order, the same shall be binding on the company, all the creditors, or class of creditors or members or class of members, as the case may be, or, in case of a company being wound-up, on the liquidator appointed under this Act or under the Insolvency and Bankruptcy Code, 2016, as the case may be and the contributories of the company.

Sub-section (7): Order of the tribunal sanctioning the scheme to provide for the certain matters

An order made by the Tribunal shall provide for all or any of the following matters, namely:

(a) where the compromise or arrangement provides for conversion of preference shares into equity shares, such preference shareholders shall be given an option to either obtain arrears of dividend in cash or accept equity shares equal to the value of the dividend payable;

(b) the protection of any class of creditors;

(c) if the compromise or arrangement results in the variation of the shareholders' rights, it shall be given effect to under the provisions of section 48;

(d) if the compromise or arrangement is agreed to by the creditors under sub-section (6), any proceedings pending before the Board for Industrial and Financial Reconstruction established under section 4 of the Sick Industrial Companies (Special Provisions) Act,1985 shall abate;

(e) such other matters including exit offer to dissenting shareholders, if any, as are in the opinion of the Tribunal necessary to effectively implement the terms of the compromise or arrangement.

No compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company's auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133.

Sub-Section (8)

The order of the Tribunal shall be filed with the Registrar by the company within a period of thirty days of the receipt of the order.

Sub-section (9): The Tribunal may dispense with calling of meeting of creditors

Section 230 (9) states that the Tribunal may dispense with calling of a meeting of creditor or class of creditors where such creditors or class of creditors, having at least ninety percent value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement.

In the case of *Sabari Rubber Private Limited & other Ca(CAA)/1(KOB)/2022,* NCLT, *Kochi Bench, Order dated* 5th day of May, 2022 inter alia observed that While considering the power of the Tribunal to dispense with the meeting of shareholders, NCLT, *Kochi Bench* relied on the decision of the National Company Law Tribunal in the case of *Jupiter Alloys & Steel (India) Limited V. Jupiter Wagons Limited (2017 SCC Online NCLT14022)*, wherein it is stated that NCLT is empowered to dispense the meeting of shareholders by virtue of its inherent powers

vested in NCLT by Rule 11 of the NCLT Rules, 2016. The NCLT, Kolkata Bench also made an observation that High Courts used to exercise their discretion to dispense the meeting of shareholders under the Companies Act, 2013 and such decisions cannot be ignored.

Under Section 230(9) of the Companies Act, 2013, the Tribunal may dispense with calling of a meeting of Creditors or class of Creditors where such Creditors or class of Creditors, having at least 90% value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement.

Sub-Section (10)

Compromise in respect of buy back is to be in compliance with section 68. As per Section 230 (10), no compromise or arrangement in respect of any buy-back of securities under this section shall be sanctioned by the Tribunal unless such buy-back is in accordance with the provisions of section 68.

Sub-Section (11)

Section 230(11) states that any compromise or arrangement may include takeover offer made in such manner as may be prescribed. In case of listed companies, takeover offer shall be as per the regulations framed by the Securities and Exchange Board.

Companies (Compromises, Arrangements and Amalgamations) Rules, 2016

Rule 3 provides that an application under sub-section (1) of section 230 of the Act may be submitted in Form no. NCLT-1 (appended in the National Company Law Tribunal Rules, 2016) along with:—

(i) a notice of admission in Form No. NCLT-2 (appended in the National Company Law Tribunal Rules, 2016);

(ii) an affidavit in Form No. NCLT-6 (appended in the National Company Law Tribunal Rules, 2016);

(iii) a copy of scheme of compromise or arrangement, which should include disclosures as per sub-section (2) of section 230 of the Act and certified true copies of all the enclosures; and

(iv) fee as prescribed in the Schedule of Fees.

(2) Where more than one company is involved in a scheme in relation to which an application under sub-rule (1) is being filed, such application may, at the discretion of such companies, be filed as a joint-application.

(3) Where the company is not the applicant, a copy of the notice of admission and of the affidavit shall be served on the company, or, where the company is being wound up, on its liquidator, not less than fourteen days before the date fixed for the hearing of the notice of admission.

(4) The applicant shall also disclose to the Tribunal in the application under sub-rule (1), the basis on which each class of members or creditors has been identified for the purposes of approval of the scheme.

(5) A member of the company shall make an application for arrangement, for the purpose of takeover offer in terms of sub-section (11) of section 230, when such member along with any other member holds not less than three-fourths of the shares in the company, and such application has been filed for acquiring any part of the remaining shares of the company.

Explanation I. "shares" means the equity shares of the company carrying voting rights, and includes any securities, such as depository receipts, which entitles the holder thereof to exercise voting rights.

Explanation II. Nothing in this sub-rule shall apply to any transfer or transmission of shares through a contract, arrangement or succession, as the case may be, or any transfer made in pursuance of any statutory or regulatory requirement.

(6) An application of arrangement for takeover offer shall contain:

(a) the report of a registered valuer disclosing the details of the valuation of the shares proposed to be acquired by the member after taking into account the following factors:

(i) the highest price paid by any person or group of persons for acquisition of shares during last twelve months;

(ii) the fair price of shares of the company to be determined by the registered valuer after taking into account valuation parameters including return on net worth, book value of shares, earning per share, price earning multiple vis-d-vis the industry average, and such other parameters as are customary for valuation of shares of such companies.

(b) details of a bank account, to be opened separately, by the member wherein a sum of amount not less than one-half of total consideration of the takeover offer is deposited.

Rule 4 provides that for the purposes of sub-clause (i) of clause (c) of sub-section (2) of section 230 of the Act, the creditor's responsibility statement in Form No. CAA. 1 shall be included in the scheme of corporate debt restructuring.

Explanation:— For the purpose of this rule, it is clarified that a scheme of corporate debt restructuring as referred to in clause (c) of sub-section (2) of section 230 of the Act shall mean a scheme that restructures or varies the debt obligations of a company towards its creditors.

Rule 6 provides that

(1) Where a meeting of any class or classes of creditors or members has been directed to be convened, the notice of the meeting pursuant to the order of the Tribunal to be given in the manner provided in sub-section (3) of section 230 of the Act shall be in Form No. CAA.2 and shall be sent individually to each of the creditors or members.

(2) The notice shall be sent by the Chairperson appointed for the meeting, or, if the Tribunal so directs, by the company (or its liquidator), or any other person as the Tribunal may direct, by registered post or speed post or by courier or by e-mail or by hand delivery or any other mode as directed by the Tribunal to their last known address at least one month before the date fixed for the meeting.

Explanation: - It is hereby clarified that the service of notice of meeting shall be deemed to have been effected in case of delivery by post, at the expiration of forty eight hours after the letter containing the same is posted.

(3) The notice of the meeting to the creditors and members shall be accompanied by a copy of the scheme of compromise or arrangement and a statement disclosing the following details of the compromise or arrangement, if such details are not already included in the said scheme:—

(i) details of the order of the Tribunal directing the calling, convening and conducting of the meeting:

(a) date of the Order;

(b) date, time and venue of the meeting.

(ii) details of the company including:

(a) Corporate Identification Number (CIN) or Global Location Number (GLN) of the company;

(b) Permanent Account Number (PAN);

(c) name of the company;

(d) date of incorporation;

(e) type of the company (whether public or private or one-person company);

(f) registered office address and e-mail address;

(g) summary of main object as per the memorandum of association; and main business carried on by the company;

(h) details of change of name, registered office and objects of the company during the last five years;

(i) name of the stock exchange (s) where securities of the company are listed, if applicable;

(j) details of the capital structure of the company including authorised, issued, subscribed and paid up share capital; and

(k) names of the promoters and directors along with their addresses.

(iii) if the scheme of compromise or arrangement relates to more than one company, the fact and details of any relationship subsisting between such companies who are parties to such scheme of compromise or arrangement, including holding, subsidiary or of associate companies;

(iv) the date of the board meeting at which the scheme was approved by the board of directors including the name of the directors who voted in favour of the resolution, who voted against the resolution and who did not vote or participate on such resolution;

(v) explanatory statement disclosing details of the scheme of compromise or arrangement including: —

(a) parties involved in such compromise or arrangement;

(b) in case of amalgamation or merger, appointed date, effective date, share exchange ratio (if applicable) and other considerations, if any;

(c) summary of valuation report (if applicable) including basis of valuation and fairness opinion of the registered valuer, if any, and the declaration that the valuation report is available for inspection at the registered office of the company;

(d) details of capital or debt restructuring, if any;

(e) rationale for the compromise or arrangement;

(f) benefits of the compromise or arrangement as perceived by the Board of directors to the company, members, creditors and others (as applicable);

(g) amount due to unsecured creditors.

(vi) disclosure about the effect of the compromise or arrangement on:

(a) key managerial personnel;

(b) directors;

(c) promoters;

(d) non-promoter members;

(e) depositors;

(f) creditors;

(g) debenture holders;

(h) deposit trustee and debenture trustee;

(i) employees of the company;

(vii) Disclosure about effect of compromise or arrangement on material interests of directors, Key Managerial Personnel (KMP) and debenture trustee.

Explanation- For the purposes of these rules it is clarified that-

(a) the term 'interest' extends beyond an interest in the shares of the company, and is with reference to the proposed scheme of compromise or arrangement.

(b) the valuation report shall be made by a registered valuer, and till the registration of persons as valuers is prescribed under section 247 of the Act, the valuation report shall be made by an independent merchant banker who is registered with the Securities and Exchange Board or an independent chartered accountant in practice having a minimum experience of ten years.

(viii) investigation or proceedings, if any, pending against the company under the Act.

(ix) details of the availability of the following documents for obtaining extract from or for making or obtaining copies of or for inspection by the members and creditors, namely:

(a) latest audited financial statements of the company including consolidated financial statements;

(b) copy of the order of Tribunal in pursuance of which the meeting is to be convened or has been dispensed with;

(c) copy of scheme of compromise or arrangement;

(d) contracts or agreements material to the compromise or arrangement;

(e) the certificate issued by Auditor of the company to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the Accounting Standards prescribed under section 133 of the Companies Act, 2013; and

(f) such other information or documents as the Board or Management believes necessary and relevant for making decision for or against the scheme;

(x) details of approvals, sanctions or no-objection(s), if any, from regulatory or any other governmental authorities required, received or pending for the proposed scheme of compromise or arrangement.

(xi) a statement to the effect that the persons to whom the notice is sent may vote in the meeting either in person or by proxies, or where applicable, by voting through electronic means.

Explanation- For the purposes of this rule, disclosure required to be made by a company shall be made in respect of all the companies, which are part of the compromise or arrangement.

Rule 7 provides that the notice of the meeting under sub-section (3) of section 230 of the Act shall be advertised in Form No. CAA.2 in at least one English newspaper and in at least one vernacular newspaper having wide circulation in the State in which the registered office of the company is situated, or such newspapers as may be directed by the Tribunal and shall also be placed, not less than thirty days before the date fixed for the meeting, on the website of the company (if any) and in case of listed companies also on the website of the SEBI and the recognized stock exchange where the securities of the company are listed:

Provided that where separate meetings of classes of creditors or members are to be held, a joint advertisement for such meetings may be given.

Rule 8 provides that for the purposes of sub-section (5) of section 230 of the Act, the notice shall be in Form No. CAA.3, and shall be accompanied with a copy of the scheme of compromise or arrangement, the explanatory statement and the disclosures mentioned under rule 6, and shall be sent to.-

i. the Central Government, the Registrar of Companies, the Income-tax authorities, in all cases;

ii. the Reserve Bank of India, the Securities and Exchange Board of India, the Competition Commission of India, and the stock exchanges, as may be applicable;

iii. other sectoral regulators or authorities, as required by Tribunal.

(2) The notice to the authorities mentioned in sub-rule (1) shall be sent forthwith, after the notice is sent to the members or creditors of the company, by registered post or by speed post or by courier or by hand delivery at the office of the authority.

(3) If the authorities referred to under sub-rule (1) desire to make any representation under sub-section (5) of section 230, the same shall be sent to the Tribunal within a period of thirty days from the date of receipt of such notice and copy of such representation shall simultaneously be sent to the concerned companies and in case no representation is received within the stated period of thirty days by the Tribunal, it shall be presumed that the authorities have no representation to make on the proposed scheme of compromise or arrangement.

Section 231 – Power of the Tribunal to enforce compromise or arrangement

As per section 231(1) when the Tribunal makes an order under section 230 sanctioning a compromise or an arrangement in respect of a company, it –

(a) shall have power to supervise the implementation of the compromise or arrangement; and

(b) may, at the time of making such order or at any time thereafter, give such directions in regard to any matter or make such modifications in the compromise or arrangement as it may consider necessary for the proper implementation of the compromise or arrangement.

Sub-section (2) states that if the Tribunal is satisfied that the compromise or arrangement sanctioned under section 230 cannot be implemented satisfactorily with or without modifications, and the company is unable to pay its debts as per the scheme, it may make an order for winding-up the company and such an order shall be deemed to be an order made under section 273.

In the case of HT Mobile Solutions Ltd. & Anr.(Appellants) vs. Regional Director, Ministry of Corporate Affairs & Ors.(Respondents), Comp. App. (AT) No. 74 of 2023 judgement dated March 12, 2024, the Hon'ble National Company Law Appellate Tribunal inter alia observed that Section 231(1) (b) of the Companies Act duly empowers the Ld. NCLT to exercise discretion to "give such directions in regard to any matter or make such modifications in the compromise or arrangement as it may consider necessary for the proper implementation of the compromise or arrangement". The Ld. NCLT was thus duly vested with sufficient powers under the Companies Act, to even partly sanction the scheme.

During the argument, the reliance was also placed on 'Rama Investment Company Pvt. Ltd. vs. Ankit Mittal' wherein vide order dated 07.09.2022 in Civil Appeal Nos. 2022-2023/2022 the Hon'ble Supreme Court was pleased to set aside the order of this Tribunal and confirm the scheme of amalgamation in part as approved by the Ld. NCLT.

Section 232 – Merger and amalgamation of companies

Sub-section (1): Tribunal's power to call meeting of creditors or members, with respect to merger or amalgamation of companies

Section 232(1) states that when an application is made to the Tribunal under section 230 for the sanctioning of a compromise or an arrangement proposed between a company and any such persons as are mentioned in that section, and it is shown to the Tribunal —

(a) that the compromise or arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of the company or companies involving merger or the amalgamation of any two or more companies; and

(b) that under the scheme, the whole or any part of the undertaking, property or liabilities of any company (hereinafter referred to as the transferor company) is required to be transferred to another company (hereinafter referred to as the transferee company), or is proposed to be divided among and transferred to two or more companies, the Tribunal may on such application, order a meeting of the creditors or class of creditors or the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal may direct and the provisions of sub-sections (3) to (6) of section 230 shall apply mutatis mutandis.

Sub-section (2): Circulation of documents for members/creditors meeting

Section 232(2) states that when an order has been made by the Tribunal under sub-section (1), merging companies or the companies in respect of which a division is proposed, shall also be required to circulate the following for the meeting so ordered by the Tribunal, namely:

(a) the draft of the proposed terms of the scheme drawn up and adopted by the directors of the merging company;

(b) confirmation that a copy of the draft scheme has been filed with the Registrar;

(c) a report adopted by the directors of the merging companies explaining effect of compromise on each class of shareholders, key managerial personnel, promoters and non-promoter shareholders laying out in particular the share exchange ratio, specifying any special valuation difficulties;

(d) the report of the expert with regard to valuation, if any;

(e) a supplementary accounting statement if the last annual accounts of any of the merging company relate to a financial year ending more than six months before the first meeting of the company summoned for the purposes of approving the scheme.

Sub-section (3): Sanctioning of scheme by Tribunal

Section 232(3) states that the Tribunal, after satisfying itself that the procedure specified in sub-sections (1) and (2) has been complied with, may, by order, sanction the compromise or arrangement or by a subsequent order, make provision for the following matters, namely:—

(a) the transfer to the transferee company of the whole or any part of the undertaking, property or liabilities of the transferor company from a date to be determined by the parties unless the Tribunal, for reasons to be recorded by it in writing, decides otherwise;

(b) the allotment or appropriation by the transferee company of any shares, debentures, policies or other like instruments in the company which, under the compromise or arrangement, are to be allotted or appropriated by that company to or for any person:

No transferee company can hold shares in its own name or under any trust.

A transferee company shall not, as a result of the compromise or arrangement, hold any shares in its own name or in the name of any trust whether on its behalf or on behalf of any of its subsidiary or associate companies and any such shares shall be cancelled or extinguished;

(c) the continuation by or against the transferee company of any legal proceedings pending by or against any transferor company on the date of transfer;

(d) dissolution, without winding-up, of any transferor company;

(e) the provision to be made for any persons who, within such time and in such manner as the Tribunal directs, dissent from the compromise or arrangement;

(f) where share capital is held by any non-resident shareholder under the foreign direct investment norms or guidelines specified by the Central Government or in accordance with any law for the time being in force, the allotment of shares of the transferee company to such shareholder shall be in the manner specified in the order;

(g) the transfer of the employees of the transferor company to the transferee company;

(h) when the transferor company is a listed company and the transferee company is an unlisted company,— the transferee company shall remain an unlisted company until it becomes a listed company; if shareholders of the transferor company decide to opt out of the transferee company, provision shall be made for payment of the value of shares held by them and other benefits in accordance with a pre- determined price formula or after a valuation is made, and the arrangements under this provision may be made by the Tribunal: The amount of payment or valuation under this clause for any share shall not be less than what has been specified by the Securities and Exchange Board under any regulations framed by it;

(i) where the transferor company is dissolved, the fee, if any, paid by the transferor company on its authorised capital shall be set-off against any fees payable by the transferee company on its authorised capital subsequent to the amalgamation; and

(j) such incidental, consequential and supplemental matters as are deemed necessary to secure that the merger or amalgamation is fully and effectively carried out.

No compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company's auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133.

Sub-section (4): Transfer of property or liabilities

Sub-section (4) states that an order under this section provides for the transfer of any property or liabilities, then, by virtue of the order, that property shall be transferred to the transferee company and the liabilities shall be transferred to and become the liabilities of the transferee company and any property may, if the order so directs, be freed from any charge which shall by virtue of the compromise or arrangement, cease to have effect

Sub-section (5): Certified copy of the order to be filed with the registrar.

Section 232(5) states that every company in relation to which the order is made shall cause a certified copy of the order to be filed with the Registrar for registration within thirty days of the receipt of certified copy of the order.

Sub Section (6): Effective date of the scheme.

Section 232(6) states that the scheme under this section shall clearly indicate an appointed date from which it shall be effective and the scheme shall be deemed to be effective from such date and not at a date subsequent to the appointed date.

Clarification issued by MCA vide General Circular No. 09/2019 dated 21st August, 2019

Clarification has been sought on whether it is mandatory to indicate a specific calendar date as 'appointed date' in the schemes referred to in the section. Further, requests have also been received to confirm whether the, acquisition date' for the purpose of Ind-AS 103 (Business combinations) would be the 'appointed date' referred to in section 232(6).

In *Marshall Sons & Co. India Ltd. v. ITO 1223 [ITR 8091]*, it was held by the Hon'ble Supreme Court that every scheme of amalgamation has to necessarily provide a date with effect from which the amalgamation/transfer shall take place, and that such date may precede the date of sanctioning of the scheme by the Court, the date of filing of certified copies of the orders of the Court before the Registrar of Companies, and the date of

allotment of shares, etc. It was observed therein that, the scheme, however, would be given effect from the transfer date (appointed date) itself.

In another case, in the matter of amalgamation of *Equitas Housing Finance Limited and Equitas Micro Finance Limited with Equitas Finance Limited* in C.P. Nos. 119 to 121 of 2016, the Hon'ble Madras High Court held that the provisions of section 394 (1) of the Companies Act, 1956 (corresponding to section 232 of the Companies Act, 2013) provided enough leeway to a company to delay the date on which the scheme of amalgamation shall take effect and tie the same to the occurrence of an event. Thus, the Court rejected the argument that the 'appointed date' in the scheme should necessarily be a specific calendar date.

Section 232(6) of the Act states that the scheme shall be deemed to be effective from the 'appointed date' and not a date subsequent to the 'appointed date'. This is an enabling provision to allow the companies to decide and agree upon an 'appointed date' from which the scheme shall come into force.

In view of the above, it was clarified that:

(a) The provision of section 232(6) of the Act enables the companies in question to choose and state in the scheme an 'appointed date'. This date may be a specific calendar date or may be tied to the occurrence of an event such as grant of license by a competent authority or fulfillment of any preconditions agreed upon by the parties, or meeting any other requirement as agreed upon between the parties, etc., which are relevant to the scheme.

(b) The 'appointed date' identified under the scheme shall also be deemed to be the 'acquisition date' and date of transfer of control for the purpose of conforming to accounting standards (including Ind-AS 103 Business Combinations.

(c) where the 'appointed date' is chosen as a specific calendar date, it may precede the date of filing of the application for scheme of merger/amalgamation in NCLT. However, if the 'appointed date' is significantly ante-dated beyond a year from the date of filing, the justification for the same would have to be specifically brought out in the scheme and it should not be against public interest.

(d) The scheme may identify the 'appointed date' based on the occurrence of a trigger event which is key to the proposed scheme and agreed upon by the parties to the scheme. This event would have to be indicated in the scheme itself upon occurrence of which the scheme would become effective. However in case of such event based date being a date subsequent to the date of filing the order with the Registrar under section 232(5), the company shall file an intimation of the same with the Registrar within 30 days of such scheme coming into force.

Sub-section (7): Annual statement certified by CA/CS/CWA to be filed with Registrar every year until the completion of the scheme.

Section 232(7) states that every company in relation to which the order is made shall, until the completion of the scheme, file a statement in such form and within such time as may be prescribed with the Registrar every year duly certified by a chartered accountant or a cost accountant or a company secretary in practice indicating whether the scheme is being complied with in accordance with the orders of the Tribunal or not.

Sub-section (8): Penal Provision:

If a company fails to comply with sub-section (5), the company and every officer of the company who is in default shall be liable to a penalty of twenty thousand rupees, and where the failure is a continuing one, with a further penalty of one thousand rupees for each day after the first during which such failure continues, subject to a maximum of three lakh rupees.

Section 233 –Merger or amalgamation of certain companies

Section 233 prescribes simplified procedure for Merger or amalgamation of

- two or more small companies, or

- between a holding company and its wholly-owned subsidiary company, or
- such other class or classes of companies as maybe prescribed.

As per rule 25(1)(1A) of Companies (Compromises, Arrangements and Amalgamations) Amendment Rules, 2021, a scheme of merger or amalgamation under section 233 of the Act may be entered into between any of the following class of companies, namely:-

(i) two or more start-up companies; or

(ii) one or more start-up company with one or more small company.

Explanation.- For the purposes of this sub-rule, "start-up company" means a private company incorporated under the Companies Act, 2013 or Companies Act, 1956 and recognized as such in accordance with notification number G.S.R. 127 (E), dated the 19th February, 2019 issued by the Department for Promotion of Industry and Internal Trade.

Sub-section (1)

Accordingly sub-section(1) of Section 233 states that notwithstanding the provisions of section 230 and section 232, a scheme of merger or amalgamation may be entered into between two or more small companies or between a holding company and its wholly-owned subsidiary company or such other class or classes of companies as may be prescribed, subject to the following, namely:—

(a) a notice of the proposed scheme inviting objections or suggestions, if any, from the Registrar and Official Liquidators where registered office of the respective companies are situated or persons affected by the scheme within thirty days is issued by the transferor company or companies and the transferee company;

(b) the objections and suggestions received are considered by the companies in their respective general meetings and the scheme is approved by the respective members or class of members at a general meeting holding at least ninety percent of the total number of shares;

(c) each of the companies involved in the merger files a declaration of solvency, in the prescribed form, with the Registrar of the place where the registered office of the company is situated; and

(d) the scheme is approved by majority representing nine-tenths in value of the creditors or class of creditors of respective companies indicated in a meeting convened by the company by giving a notice of twenty- one days along with the scheme to its creditors for the purpose or otherwise approved in writing.

Sub-section (2): The sub-section states that the transferee company shall file a copy of the scheme so approved in the manner as may be prescribed, with the Central Government, Registrar and the Official Liquidator where the registered office of the company is situated.

Sub-section (3): Central Government to issue confirmation order, where there are no objections or suggestions from registrar or official liquidator.

Section 233(3) states that on the receipt of the scheme, if the Registrar or the Official Liquidator has no objections or suggestions to the scheme, the Central Government shall register the same and issue a confirmation thereof to the companies.

Sub-section (4): Objections if any by the registrar or official liquidator to be communicated to the central government.

Section 233(4) If the Registrar or Official Liquidator has any objections or suggestions, he may communicate the same in writing to the Central Government within a period of thirty days. If no such communication is made, it shall be presumed that he has no objection to the scheme.

Sub-section (5): Application by Central Government to the Tribunal.

Section 233(5) states that if the Central Government after receiving the objections or suggestions or for any reason is of the opinion that such a scheme is not in public interest or in the interest of the creditors, it may file an application before the Tribunal within a period of sixty days of the receipt of the scheme under sub-section (2) stating its objections and requesting that the Tribunal may consider the scheme under section 232.

Sub-section (6): Tribunal's action to Central Government's application

Section 233(6) states that on receipt of an application from the Central Government or from any person, if the Tribunal, for reasons to be recorded in writing, is of the opinion that the scheme should be considered as per the procedure laid down in section 232, the Tribunal may direct accordingly or it may confirm the scheme by passing such order as it deems fit: If the Central Government does not have any objection to the scheme or it does not file any application under this section before the Tribunal, it shall be deemed that it has no objection to the scheme.

Sub-section (7): Registrar having jurisdiction over transferee company has to be communicated

Section 233(7) states that a copy of the order under sub-section (6) confirming the scheme shall be communicated to the Registrar having jurisdiction over the transferee company and the persons concerned and the Registrar shall register the scheme and issue a confirmation thereof to the companies and such confirmation shall be communicated to the Registrars where transferor company or companies were situated.

Sub-section (8): Effect of Registration of the scheme.

Sub-Section (8) states that the registration of the scheme under sub-section (3) or sub-section (7) shall be deemed to have the effect of dissolution of the transferor company without process of winding up.

Sub-section (9)

This sub-section states that the registration of the scheme shall have the following effects, namely:—

(a) transfer of property or liabilities of the transferor company to the transferee company so that the property becomes the property of the transferee company and the liabilities become the liabilities of the transferee company;

(b) the charges, if any, on the property of the transferor company shall be applicable and enforceable as if the charges were on the property of the transferee company;

(c) legal proceedings by or against the transferor company pending before any court of law shall be continued by or against the transferee company; and

(d) where the scheme provides for purchase of shares held by the dissenting shareholders or settlement of debt due to dissenting creditors, such amount, to the extent it is unpaid, shall become the liability of the transferee company.

Sub-section (10): Transferee Company not to hold any share in its own name or trust and all such shares are to be cancelled or extinguished

Section 233(10) states that a transferee company shall not on merger or amalgamation, hold any shares in its own name or in the name of any trust either on its behalf or on behalf of any of its subsidiary or associate company and all such shares shall be cancelled or extinguished on the merger or amalgamation.

Sub-section (11): Transferee Company to file an application with Registrar along with the scheme registered

The transferee company shall file an application with the Registrar along with the scheme registered, indicating the revised authorised capital and pay the prescribed fees due on revised capital. The fee, if any, paid by the transferor company on its authorised capital prior to its merger or amalgamation with the transferee company shall be set-off against the fees payable by the transferee company on its authorised capital enhanced by the merger or amalgamation.

Section 234: Merger or amalgamation of a company with a foreign company

Section 234(1) states that the provisions of this Chapter XV of the Companies Act, 2013 unless otherwise provided under any other law for the time being in force, shall apply *mutatis mutandis* to schemes of mergers and amalgamations between companies registered under this Act and companies incorporated in the jurisdictions of such countries as may be notified from time to time by the Central Government. The Central Government may make rules, in consultation with the Reserve Bank of India, in connection with mergers and amalgamations provided under this section.

Section 234(2) states that subject to the provisions of any other law for the time being in force, a foreign company, may with the prior approval of the Reserve Bank of India, merge into a company registered under this Act or vice versa and the terms and conditions of the scheme of merger may provide, among other things, for the payment of consideration to the share holders of the merging company in cash, or in Depository Receipts, or partly in cash and partly in Depository Receipts, as the case may be, as per the scheme to be drawn up for the purpose. For the purposes of sub-section(2), the expression "foreign company" means any company or body corporate incorporated outside India whether having a place of business in India or not.

Section235: Power to acquire shares of shareholders dissenting from scheme or contract approved by majority

Section 235 of the Companies Act, 2013 prescribes the manner of acquisition of shares of shareholders dissenting from the scheme or contract approved by the majority shareholders holding not less than nine tenth in value of the shares, whose transfer is involved. It includes notice to dissenting shareholders, application to dissenting shareholders to tribunal, deposit of consideration received by the transferor company in a separate bank account etc.

Section 236: Purchase of minority shareholding

Section 236 prescribes the manner of notification by the acquirer (majority) to the company, offer to minority for buying their shares, deposit an amount equal to the value of shares to be acquired, valuation of shares by registered valuer, etc.

Section 237: Power of Central Government to provide for amalgamation of companies in public interest

Section 237(1) states that when the Central Government is satisfied that it is essential in the public interest that two or more companies should amalgamate, the Central Government may, by order notified in the Official Gazette, provide for the amalgamation of those companies into a single company with such constitution, with such property, powers, rights, interests, authorities and privileges, and with such liabilities, duties and obligations, as may be specified in the order.

Continuation of legal proceedings

Section 237(2) states that the order under sub-section (1) may also provide for the continuation by or against the transferee company of any legal proceedings pending by or against any transfer or company and such consequential, incidental and supplemental provisions as may, in the opinion of the Central Government, be necessary to give effect to the amalgamation.

Interest or rights of members, creditors, debenture holders not to be affected.

As per Section 237(3), every member or creditor, including a debenture holder, of each of the transferor companies before the amalgamation shall have, as nearly as may be, the same interest in or rights against the transferee company as he had in the company of which he was originally a member or creditor, and in case the interest or rights of such member or creditor in or against the transferee company are less than his interest in or rights against the original company, he shall be entitled to compensation to that extent, which shall be assessed by such authority as may be prescribed and every such assessment shall be published in the Official Gazette, and the compensation so assessed shall be paid to the member or creditor concerned by the transferee company.

Sub-section 4: Appeal to Tribunal

As per Section 237(4) any person aggrieved by any assessment of compensation made by the prescribed authority under sub-section (3) may, within a period of thirty days from the date of publication of such assessment

in the Official Gazette, prefer an appeal to the Tribunal and thereupon the assessment of the compensation shall be made by the Tribunal.

Sub-section 5: Conditions for order

As per Section 237 (5) No order shall be made under this section unless —

(a) a copy of the proposed order has been sent in draft to each of the companies concerned;

(b) the time for preferring an appeal under sub-section (4) has expired, or where any such appeal has been preferred, the appeal has been finally disposed off; and

(c) the Central Government has considered, and made such modifications, if any, in the draft order as it may deem fit in the light of suggestions and objections which may be received by it from any such company within such period as the Central Government may fix in that behalf, not being less than two months from the date on which the copy aforesaid is received by that company, or from any class of share holders therein, or from any creditors or any class of creditors thereof.

Sub-section 6: Copy of order before each house of Parliament

As per Section 237(6) the copies of every order made under this section shall, as soon as may be after it has been made, be laid before each House of Parliament.

Section 238: Registration of offer of schemes involving transfer of shares

Section 238(1) states that in relation to every offer of a scheme or contract involving the transfer of shares or any class of shares in the transferor company to the transferee company under section 235, — (a) every circular containing such offer and recommendation to the members of the transferor company by its directors to accept such offer shall be accompanied by such information and in such manner as may be prescribed; (b) every such offer shall contain a statement by or on behalf of the transferee company, disclosing the steps it has taken to ensure that necessary cash will be available; and (c) every such circular shall be presented to the Registrar for registration and no such circular shall be issued until it is so registered:

Provided that the Registrar may refuse, for reasons to be recorded in writing, to register any such circular which does not contain the information required to be given under clause (a) or which sets out such information in a manner likely to give a false impression, and communicate such refusal to the parties within thirty days of the application.

Section 238(2) states that an appeal shall lie to the Tribunal against an order of the Registrar refusing to register any circular under sub-section (1).

Section 238(3) states that the director who issues a circular which has not been presented for registration and registered under clause (c) of sub-section(1), shall be liable to a penalty of one lakh rupees.

Section 239: Preservation of books and papers of amalgamated companies

As per section 239, the books and papers of a company which has been amalgamated with, or whose shares have been acquired by, another company under this Chapter shall not be disposed of without the prior permission of the Central Government and before granting such permission, that Government may appoint a person to examine the books and papers or any of them for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion or formation, or the management of the affairs, of the transferor company or its amalgamation or the acquisition of its shares.

Section 240: Liability of officers in respect of offences committed prior to merger, amalgamation, etc.

As per Section 240, notwithstanding anything in any other law for the time being in force, the liability in respect of offences committed under this Act by the officers in default, of the transferor company prior to its merger, amalgamation or acquisition shall continue after such merger, amalgamation or acquisition.

APPROVALS IN SCHEME OF AMALGAMATION

Merger or amalgamation of companies involves various issues including the regulatory approvals. These regulatory approvals are to be obtained not only from the sector in which the company is operating (for example in case of merger of two banks, RBI's approval is needed) but from other departments like Income Tax, SEBI, ROC, etc.

The companies are required to obtain following approvals in respect of the scheme of amalgamation:

(i) Authorisation

- Pre-approval authorisation about appointment of intermediaries, advisors, etc.
- Approval of Valuation Report by Audit Committee.

(ii) Approval of Board of Directors

- Approval of scheme of amalgamation by the Board of both the companies.

Board resolution should, besides approving the scheme, authorise a Director/Company Secretary/ other officer to make application to Tribunal, to sign the application and other documents and to do every thing necessary or expedient in connection therewith, including changes in the scheme.

(iii) Approval of Shareholders/Creditors, etc

Members' and creditors' approval to the scheme of amalgamation is *sine qua non* for Tribunal's sanction. This approval is to be obtained at specially convened meetings held as per Tribunal's directions [Section 230(1)]. However, the Tribunal may dispense with meetings of members/creditors [Section 230(9)].

The scheme of compromise or arrangement has to be approved as directed by the Tribunal, by–

- the members of the company; or
- the members of each class, if the company has different classes of shares; and the creditors; or
- each class of creditors, if the company has different classes of creditors.

The approval of the members and creditors (or each class of them) has to be obtained at specially convened meetings as per the Tribunal directions. An application seeking directions to call, hold and conduct meetings is made to the Tribunal, which has jurisdiction having regard to the location of the registered office of the company. The steps include:

- First motion petition before the Tribunal
- Scrutinizers report about the approval by the shareholders/creditors, etc.
- Second motion petition before the Tribunal
- Notices should be sent to various stakeholders, public inviting any objections to the scheme.

(iv) Approval of the Stock Exchanges

A listed entity desirous of undertaking a scheme of arrangement or involved in a scheme of arrangement, shall file the draft scheme of arrangement, proposed to be filed before Tribunal with the stock exchange(s).

(v) Approval of Financial Institutions

The approval of the Financial Institutions, trustees to the debenture holders and banks, investment corporations would be required if the Company has borrowed funds either as term loans, working capital requirements and/ orhave issued debentures to the public and have appointed any one of them as trustees to the debenture holders.

(vi) Approval from the Land Holders

If the land on which the factory is situated is the lease-hold land and the terms of the lease deed so specifies, the approval from the lessor will be needed.

(vii) Approval of the Tribunal

- Both companies (amalgamating as well as amalgamated) involved in a scheme of compromise or arrangement or reconstruction or amalgamation is required to seek approval of the respective Tribunal for sanctioning the scheme.
- Every amalgamation, except those, which involve sick industrial companies, requires sanction of Tribunal which has jurisdiction over the State/area where the registered office of a company is situated.
- If transferor and transferee companies are under the jurisdiction of different Tribunals, separate approvals are necessary.
- The notice of every application filed with the Tribunal has to be given to the Central Government (Regional Director, having jurisdiction of the State concerned).
- After the hearing is over, the Tribunal will pass an order sanctioning the Scheme of amalgamation, with such directions in regard to any matter and with such modifications in the Scheme as the Judge may think fit to make for the proper working of the Scheme. [Section 230; Rule 5, Companies (Compromises, Arrangements and Amalgamations) Rules, 2016].

The Tribunal under Section 230-234 of the Act is also empowered to order the transfer of undertaking, property or liabilities either wholly or in part, allotment of shares or debentures and on other supplemental and incidental matters.

(viii) Approval of Reserve Bank of India

Where the scheme of amalgamation envisages issue of shares/cash option to Non-Resident Indians, the amalgamated company is required to obtain the permission of Reserve Bank of India subject to conditions prescribed under the Regulations issued by RBI.

(ix) Approvals from Competition Commission of India (CCI)

The provisions relating to regulation of combination as provided under Sections 5 and 6 of the Competition Act, 2002 would also be required to be complied with by companies, if applicable.

FILING REQUIREMENTS IN THE PROCESS OF MERGER/AMALGAMATION

The following forms, reports, returns, etc. are required to be filed with the Registrar of Companies, SEBI and Stock Exchanges at various stages of the process of merger/amalgamation:

1. (a) when the objects clause of the memorandum of association of the transferee company is altered to provide for amalgamation/merger, for which special resolution is passed;

   (b) the company's authorised share capital is increased to enable the company to issue shares to the shareholders of the transferor company in exchange for the shares held by them in that company for which a special resolution for alteration of its articles is passed;

   (c) a special resolution is passed to authorise the Company's Board of Directors to issue shares to the shareholders of the transferor company in exchange for the shares held by them in that company; and

   (d) a special resolution authorizing the transferee company to commence the business of the transferor company or companies as soon as the amalgamation/merger becomes effective; the company should file with ROC within thirty days of passing of the aforementioned special

resolutions in the prescribed e-form. The following documents should be annexed to the said e-form: (i) certified true copies of all the special resolutions; (ii) certified true copy of the explanatory statement annexed to the notice for the general meeting at which the resolutions are passed, for registration of the resolution. This e-form should be digitally signed by Managing Director/Director/Manager or Secretary of the Company duly authorized by Board of Directors. This e-form should also be certified by Company Secretary or Chartered Accountant or Cost Accountant (in whole time practice) by digitally signing the e-form.

2. In compliance with the listing regulations, the transferee company is required to give notice to the stock exchanges where the securities of the company are listed, of the Board meeting called for the purpose of discussing and approving amalgamation.

3. In compliance with the listing regulations, the transferee company is required to give intimation to the stock exchanges where the securities of the company are listed, of the decision of the Board approving amalgamation and also the swap ratio, before such information is given to the shareholders and the media.

4. The transferee company is required to file with the Registrar of Companies, INC-28 along with a certified copy of the Tribunal's order on summons directing the convening and holding of meetings of equity shareholders/ creditors including debentures holders etc. as required under Section 230 of the Companies Act. This e-form should be digitally signed by the Managing Director or Director or Manager or Secretary of the Company duly authorized by the Board of Directors. However, in case of foreign company, the e-form should be digitally signed by an authorized representative of the company duly authorized by the Board of Directors.

   The original certified copy of the Tribunal order is also required to be submitted at the concerned ROC office simultaneously while filing INC-28, failing which the filing will not be considered and legal action will be taken.

5. In compliance with the listing regulations, the transferee company is required to simultaneously furnish to the stock exchanges where the securities of the company are listed, copy of every notice, explanatory statement, minutes of the meeting etc. sent to members of the company in respect of a general meeting in which the scheme of arrangement of merger/amalgamation is to be approved.

6. The transferee company is required to file with the Central Government notice of every application made to the Tribunal under Section 230 to 240 of the Companies Act, 2013. No notice need be given to the Central Government once again when the Tribunal proceeds to pass final order to dissolve the transferor company.

7. To file with the Registrar of Companies within thirty days of allotment of shares to the shareholders of the transferor company in lieu of the shares held by them in that company in accordance with the shares exchange ratio incorporated in the scheme of arrangement for merger/amalgamation, the return of allotment along with the prescribed filing fee as per requirements of the Act. This e-form should be digitally signed by Managing Director or Director or Manager or Secretary of the Company duly authorised by the Board of Directors. The e-form should also be certified by Company Secretary or Chartered Accountant or Company Secretary (in whole time practice) by digitally signing the e-form.

STEPS INVOLVED IN MERGER/AMALGAMATION

STEP – 1

Holding of Board Meeting

- To consider the proposal for Merger of the Company. It must be ensured that the companies under the consolidation must have a strong clause in the Memorandum of Association of their

organization to merge although their absence will not be an obstacle, but this will make things work smoothly.

- In-Principle approval for Merger
- Decide on jurisdiction of NCLT Benches
- Appointment of Registered Valuer
- Appointment of professionals such as chartered accountant in practice, consultants, lawyers etc
- Consultants to structure the Roadmap and draft the restructuring Scheme.

STEP – 2

Holding of Independent Directors Committee Meeting

- Report from the Committee of Independent Directors recommending the draft Scheme, taking into consideration, inter alia, that the scheme is not detrimental to the shareholders of the listed entity.

Holding of Audit Committee Meeting

- Valuation Report to be placed before Audit Committee.
- Audit Committee to give its recommendation on Draft scheme/ Share Entitlement Ratio, taking into consideration the Valuation Report.
- The Audit Committee report shall also comment on the following:
  - Need for the merger/demerger/amalgamation/arrangement
  - Rationale of the scheme
  - Synergies of business of the entities involved in the scheme
  - Impact of the scheme on the shareholders
  - Cost benefit analysis of the scheme.

Holding of Second Board Meeting

- Approval of Exchange Ratio
- Approval of Valuation Report
- Approval of Scheme of Arrangement
- Public Co. to file copy of Board Resolution with ROC [Section 117(3) (g) read with Section 179(3) (i)]
- Authorisations to sign documents, make representation and enter appearances
- File copy of scheme with ROC [Section 232(2)(b)]
- In-Principle approval of Sock Exchange
- Consider the Fairness Opinion of the Merchant Banker
- Accept the recommendation of Audit Committee
- Choose one of the Stock Exchange having nation-wide trading terminals as the Designated Stock Exchange.

STEP 3 – Filings, Intimations and Website Updations

- Intimation to Stock Exchange on the decision of the Board within 24 hours of the meeting
- Filing of Form No. MGT-14 to ROC in accordance with Section 179 of the Companies Act, 2013 within 30 days
- Company to submit the Draft Scheme along with documents to Stock Exchange in accordance with Regulation 37 of SEBI (LODR) Regulations, 2015, Simultaneously, the company shall upload all the following documents filed with Stock Exchange on its website;
  - (a) Draft Scheme of arrangement/ amalgamation/ merger/ reconstruction/ reduction of capital, etc.;
  - (b) Valuation Report;
  - (c) Report from the Audit Committee recommending the Draft Scheme, taking into consideration, inter alia, the Valuation Report. The Valuation Report is required to be placed before the Audit Committee of the listed entity;
  - (d) Fairness opinion by a SEBI Registered merchant banker on valuation of assets / shares done by the valuer for the listed entity and unlisted entity;
  - (e) Pre and post amalgamation shareholding pattern of unlisted entity;
  - (f) Audited financials of last 3 years (financials not being more than 6 months old) of unlisted entity;
  - (g) Auditor's Certificate;
  - (h) Detailed Compliance Report duly certified by the Company Secretary, Chief Financial Officer and the Managing Director.
- Any complaints received by the Company (i.e. Directly or Indirectly through Stock Exchange/SEBI) shall be submitted by company as 'Complaints Reports' to the stock exchanges within 7 days of expiry of 21 days from the date of filing of Draft Scheme with Stock Exchange(s).
- In case of unpaid dues / fines / penalties, the listed entity shall submit to stock exchanges a 'Report on the Unpaid Dues' which shall contain the details of such unpaid, prior to obtaining Observation Letter from stock exchanges on the draft scheme. The report on unpaid dues, shall be submitted by listed entity to the stock exchanges along with the draft scheme.

STEP 4 – FIRST MOTION APPLICATION

Preparation and filing of first motion application:

- Consent letter of shareholders and creditors by way of affidavit.
- Certificate from Chartered Accountant certifying creditors.
- Certification from auditors to the effect that the accounting treatment is in conformity with accounting standards [proviso to sec. 230(7) read with proviso to sec. 232 (3) of CA, 2013]
- Drafting of First Motion Application (NCLT 1), Notice of Admission (NCLT 2) & Affidavit (NCLT 6) - pray for dispensation of meeting.
- No dispensation- order for individual notices to the shareholders/creditors
- Copy of the scheme of compromise or arrangement
- Creditors responsibility statement (Form CAA 1) in case a compromise or arrangement is proposed between company and its creditors or between company and its members
- Advertisement in Newspaper (Form CAA-2).

Contents of First Motion Application

- Details of the Companies.
- Jurisdiction of NCLT Bench.
- Limitation
- Fact of the case including benefit, rationale, etc.
- Relief & prayer (Dispensation) – Specific prayer regarding dispensation for each meeting (in the matter of JVA Trading Private Limited)
- Relief & payer (Meeting) - Direction for service of notice, approval of Newspaper for advertisement.

Documents/ Annexure(s) to First Motion Application

Documents/ Annexures includes:

a) Memo of parties/Brief synopsis

b) Joint application

c) Affidavit verifying application

d) Board Resolution of all the Companies

e) Certificate from Chartered Accountants

f) Certificate from Auditors

g) Audited and/or unaudited financial statement of all the Companies

h) Memorandum and Article of Association of all the Companies

i) List of shareholders of all the companies along with their consent/NOC by way affidavits.

j) List of Creditors (Secured, unsecured).

k) Scheme of Arrangement

l) Copy of valuation Report

m) List of directors

n) Memorandum of Appearance & power of Attorney / Vakalatnama

o) Notice of Admission in NCLT 2.

STEP 5 - NCLT will give order on the application of the company on the following:

(a) Date, time and venue of the meeting

(b) Appointment of the Chairman

(c) Time within which the Chairman of the meetings will give his report

(d) Dispensation of meeting for the unlisted Company

The order of the Tribunal shall be filed with the Registrar by the company within a period of 30 days of the receipt of the order.

STEP 6- Notice of First Motion Application

No dispensation – Notice of meeting of arrangement or compromise shall be given to:

- Shareholders & Creditors
- Central Government
- Income Tax Authorities
- Reserve Bank of India
- Securities and Exchange Board of India
- The Registrar
- Official Liquidator
- Competition Commission of India
- Advertisement in Newspaper (Form CAA-2).

The notice to statutory authorities shall be in Form CAA 3 and shall be accompanied with a copy of the scheme of compromise or arrangement, the explanatory statement and the prescribed disclosures

STEP 7 – Holding of Meeting

Process of Meeting

- Court appointed Chairman/ Alternate Chairman to preside over.
- Quorum, as decided by the Tribunal.
- Public shareholders consent by Postal Ballot (Listed Co.) and through e-voting (if required) as per SEBI norms
- Scrutinizer, as appointed by the Tribunal
- Report of the Scrutinizer to the Chairman
- Report of the Chairman to be filed with Tribunal within the time fixed by the tribunal, or where no time has been fixed, within three days after the conclusion of the meeting submit a report to the Tribunal on the result of the meeting in Form CAA 4

STEP 8- Filing of Second Motion application

Where the proposed compromise or arrangement is agreed to by the members or creditors or both as the case maybe with or without modification, the company (or its liquidator), shall:

- Within 7 days of receipt of certified true copy of order of NCLT and / or filing of report by the Chairperson, as the case may be, the second motion petition must be filed in Form CAA.5 for sanction of the scheme praying for appropriate orders and directions under section 230 read with section 232 of the Companies Act, 2013 [Rule 15 of the Companies (Compromise, Arrangement and Amalgamation) Rule, 2016]
- Where the company fails to present the petition for confirmation of the compromise or arrangement as aforesaid, it shall be open to any creditor or member as the case may be, with the leave of the tribunal, to present the petition and the company shall be liable for the cost thereof.

STEP 9- Hearing on admission of Second Motion

- NCLT shall fix a date of hearing of the petition, and
- Order to advertise the notice of hearing in such newspaper as the NCLT may think fit, not less than 10 days before the date of hearing of petition [Rule 16 of the Companies (Compromise, Arrangement and Amalgamation) Rule, 2016]

Publish the advertisement in Form NCLT-3A, place the same on the Website, if any and file an affidavit of compliance in relation to the same, not less than 3 days before the fixed for hearing [Rule 35 of the National Company Law Tribunal Rules, 2016].

STEP 10- Approval of Regulatory Authorities

- Filing of First motion, second motion along with notice with all the authorities.
- Report of ROC to office of Regional Director.
- Query letter and its reply to office of Regional Director
- Query letter and its reply to office of official Liquidators
- Report of RD and OL to be filed with Tribunal.

STEP 11- Final Hearing

- NCLT may, if it thinks fit, sanction the scheme and pass anOrder in Form CAA 7, with such variations as the circumstance may require.

The order shall direct that a certified copy of the same shall be filed with the registrar of companies within 30 days from the date of the receipt of copy of the order, or such other time as maybe fixed by the tribunal.

STEP 12- Filing with Scheme & other Compliance

- Board Meeting to take note of the Copy of Order, fixation of records date and board meeting of Resulting Company for allotment of shares to the members of Demerged Company
- File the certified true copy of order of NCLT with ROC in From INC-28, within 30 days from the date of the receipt of certified true copy of order [Section 232(5) of the Companies Act, 2013]
- Filing of Form PAS 3, SH. 7
- Change of Name, Conversion, Consolidation of share, reclassification of share, reduction of share, if any
- Dispatch of Share Certificates to the allottees or entering the name of allottees as beneficial owner in the records of depositories
- Apply to Stock Exchange for Listing of Shares of Resulting Company within 30 Days of Receipt of Order of the NCLT sanctioning the Scheme;
- Before commencement of Trading, advertisement is required to be given in one Hindi and one English newspaper having nationwide circulation and one regional newspaper with the wide circulation at the place where the registered office of the Resulting Company is situated
- Formalities for commencement of trading shall be completed within 45 Days of the order of NCLT

STEP 13: Certification of Compliance of Scheme

- A statement (Form CAA 8) is to be filed with Registrar in regard to compliance of scheme in accordance with the orders of the Tribunal every year until the scheme is fully implemented.
- It must be certified by a chartered accountant or a cost accountant or a company secretary in practice indicating whether the Scheme is being complied in accordance with the orders of the Tribunal or not.

REVISED ORGANIZATION CHART

One modification that has great potential to affect the new business is a change in the organizational structure. Regardless of whether the changes are large or small, planningand an intense analysis are vital to creating a decision-making and communication framework that will support post-merger objectives and help the new business grow.

Structural Change Considerations

An organizational structure refers to the levels of hierarchy, chain of command, management systems and job structures and roles. In response to a merger, duplicate departments need to be merged or eliminated, and at least some employees from both companies will either transfer to new positions or leave the company. Communication patterns will typically change as managers acquire new employees and everyone adapts to changes in policies and procedures designed to fit the new company.

Premerger Due Diligence

Review the organizational structures of both businesses to see how well each compares to the mission and long-term objectives for the new company. Analyze hierarchies and reporting relationships to see where the existing structures clash and where they're synchronized. Once an initial review is completed, appoint an integration team to speak with core employees and get their perspective on what works and what doesn't work in their respective structures. Make preliminary decisions about which features best support the new business.

Structural Change Options

Organizational structure change options include starting from scratch, eliminating one in favor of the other and combining the best features of both structures into one. Which is the best option depends on the size, complexity and objectives of the new business. For example, two small businesses with flat organizational structures may need to convert to a more hierarchical and organized structure that allows for greater internal controls and division of responsibilities. It is also useful when the owners or chief executive officer delegates some decision-making responsibilities.

The Three Phases of Change

Changing an organizational structure due to a merger involves much more than creating a new organizational chart. Although the chart will reflect decisions made about how the new business's employees will communicate with one another and make decisions, this typically occurs in multiple phases. The first phase is awareness, during which employees from both businesses come to understand the new company's direction and what it will mean to them. The goal of the second phase is acceptance, as the integration team works to build new relationships and employees at every level transition into new roles and new ways of getting work done. In the final phase, the merger is complete and the new organizational structure becomes fully adopted.

For example in merger of the associate banks of SBI with that of the State Bank of India, some of the branches of the erstwhile associate banks were allowed to shift to other places or closed down. Further the Administrative offices/ Regional offices were also reorganized since these offices of the merged bank lost their identity and the authority of the existing Regional/ Zonal Offices of the acquiring bank were expanded to have control over more branches or realigned. Similarly apart from the relocation of the branches and regional/zonal offices, the authority and responsibility of the middle level and higher level officers were also realigned and tuned with the requirement after the merger.

EMPLOYEE COMPENSATION, BENEFITS AND WELFARE ACTIVITIES

Employee's compensation in the two companies varies. For example in the case of merger between the Bank of Rajasthan Ltd. (BoR) and the ICICI Bank Ltd which was held in 2010, the BoR employees were aligned with the Indian Bank Association (IBA), while the ICICI Bank was having its own compensation and not linked with the IBA compensation policy. In order to have consistency in compensation policy the merged bank employees were forced to adopt the compensation policy of the acquiring bank.

Whatever the strategy is adopted, companies need to be sensitive with regard to terms and conditions of employment. Usually, courts would uphold terms of employment to be no less favorable than existing terms and conditions. Post-acquisition, the parent company may want the acquired company to adopt compensation structure of the parent entity. It would result in re-aligning the structure as well as pay scales of existing employees.

ALIGNING COMPANY POLICIES

After merger the merged entity is usually forced to adopt the policies of the merging company. The accounting software and policies of the amalgamating companies are to be aligned with that of the amalgamated company in a phased manner. For example in the case of the merger of the two banking companies, the acquiring bank imposes its accounting software (like Finacle) on the merged bank and also various policies like Deposit Policy, Loan Policy, Recovery & Compromise Policy, etc. in order to have uniformity in serving the customers. However if the products of the erstwhile (merged) entity is good enough, the same are allowed to be continued till the conclusion of the scheme. For example, at the time of the merger of the Bank of Rajasthan Ltd (BoR) with ICICI Bank Ltd, the customers of the BoR were charged for the same service charges for some time and allowed to continue with some of the product schemes as per the sanction terms and conditions, in order to win the customer's confidence in the acquiring bank too.

ALIGNING ACCOUNTING AND INTERNAL DATABASE MANAGEMENT SYSTEMS

Besides passing appropriate accounting entries to capture the merger/ acquisition/ financial structure, the company may need to adopt accounting policies, practices based on those followed by its new parent organization post acquisition. The company needs to understand any reporting and database requirements of acquiring company or merged entity to provide relevant data to the new management and to align existing systems with those of the parent/ merged entity. This may involve providing suitable training to concerned personnel and understanding issues, if any, to avoid incorrect reporting.

RECORD KEEPING

Preservation of books and papers of amalgamated companies: Section 239 provides that the books and papers of a company which has been amalgamated with, or whose shares have been acquired by, another company shall not be disposed of without the prior permission of the Central Government and before granting such permission, that Government may appoint a person to examine the books and papers or any of them for the purpose of ascertaining whether they contain any evidence of the commission of an offence in connection with the promotion or formation, or the management of the affairs, of the transferor company or its amalgamation or the acquisition of its shares.

Maintenance of records of merging entity and making suitable entries in the records (e.g. registers under Companies Act reflecting changes in shareholding, directors etc. as applicable) of merged entity is a must. One will need to dive deep to ensure maintenance of all past records including statutory and non-statutory registers, original copies of various forms, returns, certificates, approvals, litigation and property records. Company may need to relocate the records to centralized storage maintained by the merged/new entity.

INTEGRATION OF BUSINESSES AND OPERATIONS

The integration of business and operations after merger is the crucial part and many points require attention on the issue. These may be list out as under:

- Assessment of the future cash flow generation in order to have organic growth after having gone through the process of inorganic growth.
- Integration of the accounting software, accounting policy.
- Integration of various other software.
- The customer retention of the merged entity and acquisition of more customers.
- Satisfaction of the human resources and retaining of the talent.

POST-MERGER SUCCESS AND VALUATION

Every merger is not successful. The factors which are required to measure the success of any merger are briefly discussed below:

- The earning performance of the merged company can be measured by return on total assets and return on net worth. It has been found that the probability of success or failure in economic benefits was very high among concentric mergers. Simple vertical and horizontal mergers were found successful whereas the performance of concentric mergers was in between these two extremes i.e. failure and success.
- Whether the merged company yields larger net profit than before, or a higher return on total funds employed or the merged company is able to sustain the increase in earnings.
- The capitalisation of the merged company determines its success or failure. Similarly, dividend rate and payouts also determines its success or failure.
- Whether merged company is creating a larger business organisation which survives and provides a basis for growth.
- Comparison of the performance of the merged company with the performance of similar sized company in the same business in respect of (i) Sales, (ii) assets, (iii) net profit, (iv) earning per share and (v) market price of share. In general, growth in profit, dividend payouts, company's history, and increase in size provides base for future growth and are also the factors which help in determining the success or failure of a merged company.
- Fair market value is one of the valuation criteria for measuring the success of post merger company. Fair market value is understood as the value in the hands between a willing buyer and willing seller, each having reasonable knowledge of all pertinent facts and neither being under pressure or compulsion to buy or sell. Such valuation is generally made in pre-merger cases.
- In valuing the whole enterprise, one must seek financial data of comparable companies in order to determine ratios that can be used to give an indication of the company position. The data is analyzed to estimate reasonable future earnings for the subject company. The following information must be made available and analyzed for post-merger valuation:
    - All year-end balance sheets and income statements, preferably audited, for a period of five years and the remaining period up to the valuation date.
    - All accounting control information relating to the inventory, sales, cost, and profit contribution by product line or other segment; property cost and depreciation records; executives and managerial compensation; and corporate structure.
    - All records of patents, trademarks, contracts, or other agreements.
    - A history of the company, including all subsidiaries.

Analysis of these items provides data upon which forecasts of earnings, cash flow, etc. can be made.

- Gains to shareholders have so far been measured in terms of increase or decrease in share prices of the merged company. However, share prices are influenced by many factors other than the performance results of a company. Hence, this cannot be taken in isolation as a single factor to measure the success or failure of a merged company.
- In some mergers there is not only increase in the size of the merged or amalgamated company in regard to capital base and market segments but also in its sources and resources which enable it to optimize its end earnings.
- In addition to the above factors, a more specific consideration is required to be given to factors like improved debtors realisation, reduction in non-performing assets, improvement due to economies of large scale production and application of superior management in sources and resources available relating to finance, labour and materials.

HUMAN AND CULTURAL ASPECTS

Human Aspects: The merger and acquisition in the corporate world is a common phenomenon. It may be the horizontal merger or vertical merger. A horizontal merger decreases competition in the market, while vertical merger is a merger between companies in the same industry, but at different stages of production process. However the most neglected part in the merger story is the human aspect. The employees of the amalgamated entity face secondary treatment in the amalgamating company. They are harassed, transferred recklessly and demoted one or two scale lower, which leads to frustration and are forced to take voluntary retirement. In this way the company losses the good employees too. The merger of the Bank of Rajasthan Ltd with ICICI Bank Ltd and the Associate Banks of State Bank of India with the State Bank of India are good examples, in which many of the employees of the merged entities have opted the voluntary retirement.

Cultural Aspects: Apart from the human aspects the cultural issue in the case of merger is also a crucial issue. Integration of the employees accustomed of different cultural background is a typical aspect. Implementation of structural nature may be financially and legally successful. But if cultural issues are ignored, the success may only be transient. Culture of an organisation means the sum total of things the people do and the things the people do not do. Behavioural patterns get set because of the culture. These patterns create mental blocks for the people in the organization. Pre-merger survey and summarization of varying cultures of different companies merging, needs to be carried out. People belonging to the each defined culture need to be acquainted with other cultures of other merging companies. They need to be mentally prepared to adopt the good points of other cultures and shed the blockades of their own cultures. Such an open approach will make the fusion of cultures and ethos easy and effective.

MEASURING POST-MERGER EFFICIENCY

The criterion to judge a successful merger differs in different conditions. Different factors may be considered for making value judgements such as growth in profit, dividend, company's history, increase in size, base for growth, etc. Several studies suggest different parameters to assess the success of mergers:

- Successful merger creates a larger industrial organization than before, and provides a basis for growth [Edith Perirose].
- In Arthur Dewing's study, three criteria were considered viz. (a) merger should give a larger net profit than before (b) merger should provide a higher return on total funds (c) there should be a sustained increase in earnings.
- Earnings on capitalization and dividend records determine the success of merger [Shaw L.].

During the studies in late 1960s, two types of efficiency improvements were expected to result from mergers:

(1) Improvements due to economies of large scale production

(2) Application of superior management skills to a larger organisation. Some other researches in the seventies and eighties, measure efficiency based on stock market measures, labour productivity or total factor productivity, etc. These improvements pointed towards market dominance, but for gauging efficiency, resultant profitability was accepted as a benchmark. In order to ensure progress, a conscious and concerted effort to keep track of several key elements is required, along with answers to the following questions:

1. What impact is the integration (merger/acquisition) having on key indicators of business performance? Whether synergies which were hypothesized during the valuation are being realized?
2. Are the activities and milestones developed with the integration process on target?
3. What are the major issues emerging during the integration, requiring considerable attention?
4. What important facts have emerged during the merger or acquisition that can be used to improve subsequent mergers or acquisition?

MEASURING KEY INDICATORS

The main purpose of a merger or acquisition is to deliver the expected financial results namely earnings and cash flow. However, there are certain other measures that serve as key indicators and they also need to be measured. The indicators may be grouped as:

i. Financial outcomes.

ii. Component measures of these outcomes namely revenues, costs, net working capital and capital investments.

iii. Organisational indicators such as customers, employees and operations.

All the areas being integrated and both the acquirer and target, or in a merger, both partners, should be brought within the ambit of continuous appraisal. Also, the appraisal should be based on benchmarks to ensure that merger or acquisition are yielding the financial and strategic objective so intended and are not resulting in value leakage.

There are broadly four possible reasons for business growth and expansion which is to be achieved by the merged company. These are (1) Operating economies, (2) Financial economies, (3) Growth and diversification, and (4) Managerial effectiveness.

LESSON ROUND-UP

- Chapter XV, comprising of sections 230 to 240 of the Companies Act, 2013 read with the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016, deals with Compromises, Arrangements and Amalgamations.
- Section 230 is relating to the power of the company to compromise or to make arrangement with its creditors and members.
- Section 230(2) deals with regard to information as to compromises and arrangements with creditors and members.
- Section 232 deals with facilitation of merger and amalgamation of companies.
- Sections 235-236 deal with provisions regarding the power and duty to acquire shares of shareholders dissenting from scheme or contract approved by majority shareholders.
- Section 237 contains provisions as to the power of the central government to provide for amalgamation of companies in national interest.
- Merger or amalgamation of companies involves various issues including the regulatory approvals. These regulatory approvals are to be obtained not only from the sector in which the company is operating (for example in case of merger of two banks, RBI's approval is needed) but from other departments like Income Tax, SEBI, ROC, etc.
- Due diligence is an investigation of a business or person prior to signing a contract, or an act with a certain standard of care. It can be a legal obligation, but the term will more commonly apply to voluntary investigations.
- General principles of Business Valuation are: Principle of Time Value of Money, Principle of Risk and Return, Principle of Substitution, Principle of Alternatives, Principle of Reasonableness.
- The most popular methods of valuation amongst other include Asset based valuation, Earnings based valuation and Market based valuation. Other aspects as to the Methods of Valuation are Relative Method, Super Profit Method, Contingent Claim Method, and Accounting Professionals Experts.
- 'Post-merger reorganization' is a wide term which encompasses the reorganization of each and every aspect of the company's functional areas to achieve the objectives planned and aimed at.

- There are broadly four possible reasons for business growth and expansion which is to be achieved by the merged company. These are (1) Operating economies, (2) Financial economies, (3) Growth and diversification, and (4) Managerial effectiveness.
- Human and cultural integration is central to the success of any merger.
- The earning performance of the merged company can be measured by return on total assets and return on net worth.
- In general, growth in profit, dividend pay-outs, company's history and increase in size provides the base for future growth and are also the factors which help in determining the success or failure of a merged company.

GLOSSARY

Merger : An amicable involvement of two or more companies to form one unit, and to increase overall efficiency. The shareholders of merged companies are offered equivalent holdings in the new company.

Amalgamation : The joining of one or more companies into a new entity. None of the combining companies remains; a completely new legal entity is formed.

Offer Price : The price offered per share by the acquirer.

Share Exchange Ratio : The offer price divided by the acquirer's share price.

Synergy : Cost savings and revenue enhancements that are expected to be achieved in connection with a merger/acquisition.

TEST YOURSELF

(*These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation*)

1. Write a detailed note on the merger and acquisition provisions contained in the Companies Act, 2013 and its relevant rules.
2. Describe the regulatory authorities from whom the approvals are to be taken in case of merger/ amalgamation and its process.
3. Discuss the role of Tribunal in approving a scheme of reconstruction or restructuring under Sections 230-240 of the Companies Act, based on decided cases from the standpoint of shareholders and employees.
4. ABC & Co (P) Ltd. and XYZ Ltd. have finalized a scheme of arrangement. The registered offices of both the companies are located in Delhi. A joint-petition is proposed to be filed before the Tribunal for sanction of the scheme.

   Give your brief opinion in the light of the provisions of the Companies Act, 2013 and the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 whether such a joint-petition can be filed.
5. What do you understand by Due Diligence? Mention the types of due diligence and what should be the contents of the due diligence report?

LIST OF FURTHER READINGS

- Guide to Companies Act by A Ramaiya, Lexis Nexis Butterworths
- The Companies Act, 2013 with Rules and Ready Referencer by S K Kataria, Bloomsbury Publication
- Guide to Takeovers and Mergers by Sridharan and Pradhan, Wadhwa & Co.